



ENTREPRENEURSHIP

Ideas in Action

4e

Cynthia L. Greene

 SOUTH-WESTERN
CENGAGE Learning™

Australia • Brazil • Japan • Korea • Mexico • Singapore • Spain • United Kingdom • United States



**Entrepreneurship: Ideas in Action,
Fourth Edition
Cynthia L. Greene**

Vice President of Editorial, Business:
Jack W. Calhoun
Vice President/Editor-in-Chief:
Karen Schmohe
Vice President/Marketing: Bill Hendee
Executive Editor: Eve Lewis
Sr. Developmental Editor: Enid Nagel
Editorial Assistant: Virginia Wilson
Marketing Manager: Mike Cloran
Marketing Coordinator: Kelley Gilreath
Content Project Manager: Darrell E. Frye
Manager of Technology, Editorial: Liz Wilkes
Technology Project Editor: Sally Nieman
Website Project Manager: Ed Stubenrauch
Manufacturing Coordinator: Kevin Kluck
Production Service:
Macmillan Publishing Solutions
Art Director: Tippy McIntosh
Internal and Cover Designer:
Grannan Design, Ltd
Cover Images: Veer, PhotoAlto/Getty
Photography Manager: John Hill

© 2009, 2006 South-Western, a part of Cengage Learning

ALL RIGHTS RESERVED. No part of this work covered by the copyright herein may be reproduced, transmitted, stored or used in any form or by any means graphic, electronic, or mechanical, including but not limited to photocopying, recording, scanning, digitizing, taping, Web distribution, information networks, or information storage and retrieval systems, except as permitted under Section 107 or 108 of the 1976 United States Copyright Act, without the prior written permission of the publisher

For product information and technology assistance, contact us at
Cengage Learning Customer & Sales Support, 1-800-354-9706

For permission to use material from this text or product,
submit all requests online at www.cengage.com/permissions
Further permissions questions can be emailed to
permissionrequest@cengage.com

ExamView® and **ExamView Pro®** are registered trademarks of FSCreations, Inc.

The Career Clusters icons are being used with permission of the:



States' Career Clusters Initiative, 2007, www.careerclusters.org

© 2008 Cengage Learning. All Rights Reserved.

Student Edition ISBN 13: 978-0-538-44614-3

Student Edition ISBN 10: 0-538-44614-5

Student Edition with CD ISBN 13: 978-0-538-44626-6

Student Edition with CD ISBN 10: 0-538-44626-9

South-Western Cengage Learning
5191 Natorp Boulevard
Mason, OH 45040
USA

Cengage Learning products are represented in Canada by
Nelson Education, Ltd.

For your course and learning solutions, visit school.cengage.com



Reviewers

Tatyana Berkovich

President and Founder
Ivy Academia
K-12th grade Entrepreneurial Charter School
Woodland Hills, California

Becky Bernard

Coordinator/Instructor, Small Business
Vanguard Sentinel Adult Career Centers
Fremont, Ohio

Julie Carney

Program Manager
NFIB Young Entrepreneur Foundation
Washington, DC

Pat Edwards

Instructor, Hospitality Management
Fairfax County Public Schools
Chantilly Academy
Chantilly, Virginia

Mary A. Fugate

Business Education/OJT Instructor
Grants High School
Grants, New Mexico

Roger H. Fulk

Professor, Office Information Systems
Wright State University—Lake Campus
Celina, Ohio

Arlene Gibson

Director, Office of Career and
Technical Education
Career and Technical Education
Detroit Public Schools
Detroit, Michigan

Michael Hackman

Teacher, Business Department
Columbus North High School
Columbus, Indiana

Catherine Hayes

Teacher
Culinary Arts & Entrepreneurship
Albuquerque Public Schools
Del Norte High School
Albuquerque, New Mexico

Linda Hughes

Business Educator
Rapides High School
Lecompte, Louisiana

Susan Krebsbach

Teacher
Broken Arrow High School
Broken Arrow, Oklahoma

Carol T. Majors

Consultant
Consortium for Entrepreneurship Education
Lee's Summit, Missouri

Azzie L. Olds

Business Instructor
North Caddo Magnet High School
Vivian, Louisiana

Michael Vialpando

Business Department Chair
La Joya Community High School
Phoenix, Arizona

Kim Watson

Marketing Teacher
The Academy of Irving
Irving, Texas

Jasper L. Wilson

Business Education Supervisor
Prince George's County Public Schools
Upper Marlboro, Maryland

Contents



Should You Become an Entrepreneur? 2

Ideas in Action Making Job Connections 3

- 1-1 All about Entrepreneurship 4
- 1-2 Is Entrepreneurship Right for You? 10
- 1-3 Exploring Ideas and Opportunities 16
- 1-4 Problem Solving for Entrepreneurs 21

Be Your Own Boss 19
Develop Your Reading Skills 5
Did You Know? 11
Famous Entrepreneur 7
Net Bookmark 17
Teamwork 9, 15, 20, 25
What Went Wrong? 13

Lesson Assessment 9, 15, 20, 25

Chapter Assessment 28

Build Your Business Plan Project 31

Sharpen Your Entrepreneurial Skills

Effective Business Letters 26

Planning a Career in

Human Services 32

Winning Edge

BPA Presentation Management Team 33



Entrepreneurs in a Market Economy 34

Ideas in Action Web Site Design 35

- 2-1 Entrepreneurs Satisfy Needs and Wants 36
- 2-2 How Economic Decisions Are Made 42
- 2-3 What Affects Price? 49

Be Your Own Boss 47
Develop Your Reading Skills 37
Did You Know? 46
Famous Entrepreneur 44
Net Bookmark 38
Teamwork 41, 48, 54
What Went Wrong? 53

Lesson Assessment 41, 48, 54

Chapter Assessment 56

Build Your Business Plan Project 59

Sharpen Your Entrepreneurial Skills

Effective Presentation Skills 55

Planning a Career in

Property Management 60

Winning Edge

FBLA Emerging Business Issues Event 61



Develop a Business Plan 62

Ideas in Action Turning an Idea into a Business 63

- 3-1 Why a Business Plan Is Important 64
- 3-2 What Goes into a Business Plan? 69
- 3-3 How to Create an Effective Business Plan 78

Be Your Own Boss 80

Develop Your Reading Skills 65

Did You Know? 79

Famous Entrepreneur 67

Net Bookmark 81

Teamwork 68, 77, 82

What Went Wrong? 72

Lesson Assessment 68, 77, 82

Chapter Assessment 84

Build Your Business Plan Project 87

Sharpen Your Entrepreneurial Skills

Using Technology Tools 83

Planning a Career in

Landscape Architecture 88

Winning Edge

BPA Prepared Speech 89



Identify and Meet a Market Need 90

Ideas in Action Serving Customers' Needs 91

- 4-1** Identify Your Market 92
- 4-2** Research the Market 97
- 4-3** Know Your Competition 104
 - Be Your Own Boss 107
 - Develop Your Reading Skills 93
 - Did You Know? 99
 - Famous Entrepreneur 98
 - Net Bookmark 101
 - Teamwork 96, 103, 110
 - What Went Wrong? 94
 - Lesson Assessment 96, 103, 110
 - Chapter Assessment 112
 - Build Your Business Plan Project 115
 - Sharpen Your Entrepreneurial Skills
 - Using Spreadsheets to Analyze Data 111
 - Planning a Career in
 - Marketing Research 116
 - Winning Edge
 - FBLA Multimedia Presentation 117



Market Your Business 118

Ideas in Action Turning Creative Fun into Dollars 119

- 5-1** Develop the Marketing Plan 120
- 5-2** The Marketing Mix—Product 126
- 5-3** The Marketing Mix—Price 131
 - Be Your Own Boss 136
 - Develop Your Reading Skills 121
 - Did You Know? 127
 - Famous Entrepreneur 122
 - Net Bookmark 129
 - Teamwork 125, 130, 138
 - What Went Wrong? 128

- Lesson Assessment 125, 130, 138
- Chapter Assessment 140
- Build Your Business Plan Project 143
- Sharpen Your Entrepreneurial Skills

Breakeven Point 139

Planning a Career in

E-marketing 144

Winning Edge

BPA Global Marketing Team Event 145



Distribution, Promotion, and Selling 146

Ideas in Action Turning a Bad Experience into a Million Dollars 147

- 6-1** The Marketing Mix—Distribution 148
- 6-2** The Marketing Mix—Promotion 154
- 6-3** Selling and Promoting 164

Be Your Own Boss 150

Develop Your Reading Skills 149

Did You Know? 155

Famous Entrepreneur 167

Net Bookmark 157

Teamwork 153, 163, 168

What Went Wrong? 161

Lesson Assessment 153, 163, 168

Chapter Assessment 170

Build Your Business Plan Project 173

Sharpen Your Entrepreneurial Skills

Marketing and the Web 169

Planning a Career in

Public Safety 174

Winning Edge

DECA Entrepreneurship Promotion Project 175



Select a Type of Ownership 176

Ideas in Action Capitalize on Youth Marketing 177

- 7-1** Decide to Purchase, Join, or Start a Business 178
- 7-2** Choose a Legal Form of Business 187
- 7-3** Legal Issues and Business Ownership 194
 - Be Your Own Boss 192
 - Develop Your Reading Skills 179
 - Did You Know? 184
 - Famous Entrepreneur 197
 - Net Bookmark 183
 - Teamwork 186, 193, 200
 - What Went Wrong? 190
 - Lesson Assessment 186, 193, 200
 - Chapter Assessment 202
 - Build Your Business Plan Project 205
 - Sharpen Your Entrepreneurial Skills
 - Effective Telephone Conversations 201
 - Planning a Career in
 - Franchising 206
 - Winning Edge
 - DECA Business Law and Ethics Management
 - Team Decision Making Event 207



Locate and Set Up Your Business 208

Ideas in Action A Neighborhood Business 209

- 8-1** Choose a Location 210
- 8-2** Obtain Space and Design the Physical Layout 218
- 8-3** Purchase Equipment, Supplies, and Inventory 224

- Be Your Own Boss 227
- Develop Your Reading Skills 211
- Did You Know? 220
- Famous Entrepreneur 221
- Net Bookmark 222
- Teamwork 217, 223, 228
- What Went Wrong? 215
- Lesson Assessment 217, 223, 228
- Chapter Assessment 230
- Build Your Business Plan Project 233
- Sharpen Your Entrepreneurial Skills
 - E-Mail Etiquette 229
- Planning a Career in
 - Architecture and Construction 234
- Winning Edge
 - DECA Buying and Merchandising Management
 - Team Decision Making Event 235



Plan and Track Your Finances 236

Ideas in Action Electronic Safekeeping 237

- 9-1** Finance Your Business 238
- 9-2** Pro Forma Financial Statements 246
- 9-3** Recordkeeping for Businesses 253
 - Be Your Own Boss 259
 - Develop Your Reading Skills 239
 - Did You Know? 245
 - Famous Entrepreneur 243
 - Net Bookmark 244
 - Teamwork 245, 252, 260
 - What Went Wrong? 256
 - Lesson Assessment 245, 252, 260
 - Chapter Assessment 262
 - Build Your Business Plan Project 265
 - Sharpen Your Entrepreneurial Skills
 - Prepare a Resume 261
 - Planning a Career in
 - Finance 266
 - Winning Edge
 - FBLA Business Financial Plan 267



Operations Management 268

Ideas in Action Entertaining and Planning 269

- 10-1** Operating Procedures 270
- 10-2** Inventory Management 276
- 10-3** Financial Management 283
 - Be Your Own Boss 278
 - Develop Your Reading Skills 271
 - Did You Know? 284
 - Famous Entrepreneur 281
 - Net Bookmark 272
 - Teamwork 275, 282, 290
 - What Went Wrong? 285
- Lesson Assessment 275, 282, 290
- Chapter Assessment 292
- Build Your Business Plan Project 295
- Sharpen Your Entrepreneurial Skills
 - Leadership Skills 291
- Planning a Career in
 - Information Technology 296
- Winning Edge
 - FBLA Partnership with Business 297



Human Resource Management 298

Ideas in Action Working for What You Believe In 299

- 11-1** Identify Your Staffing Needs 300
- 11-2** Staff Your Business 307
- 11-3** Direct and Control Human Resources 315
 - Be Your Own Boss 316
 - Develop Your Reading Skills 301
 - Did You Know? 311
 - Famous Entrepreneur 312
 - Net Bookmark 304
 - Teamwork 306, 314, 322
 - What Went Wrong? 318

- Lesson Assessment 306, 314, 322
- Chapter Assessment 324
- Build Your Business Plan Project 327
- Sharpen Your Entrepreneurial Skills
 - Promoting Teamwork 323
- Planning a Career in
 - Audio-Video Technology 328
- Winning Edge
 - FBLA Business Plan 329



Risk Management 330

Ideas in Action Growth Is Risky 331

- 12-1** Business Risks 332
- 12-2** Insure Against Risks 338
- 12-3** Other Risks 345
 - Be Your Own Boss 336
 - Develop Your Reading Skills 333
 - Did You Know? 339
 - Famous Entrepreneur 351
 - Net Bookmark 335
 - Teamwork 337, 344, 352
 - What Went Wrong? 342
- Lesson Assessment 337, 344, 352
- Chapter Assessment 354
- Build Your Business Plan Project 357
- Sharpen Your Entrepreneurial Skills
 - Respect Cultural Diversity 353
- Planning a Career in
 - Insurance 358
- Winning Edge
 - DECA Business Services Marketing Series Event 359



Management for the Future 360

Ideas in Action **Starting Young and Moving Up 361**

- 13-1** Growth Strategies 362
- 13-2** Ethical and Social Issues 370
- 13-3** Global Trends and Opportunities 378

Be Your Own Boss 380
Develop Your Reading Skills 363
Did You Know? 375
Famous Entrepreneur 383
Net Bookmark 374
Teamwork 369, 377, 384
What Went Wrong? 364

Lesson Assessment 369, 377, 384
Chapter Assessment 386
Build Your Business Plan Project 389
Sharpen Your Entrepreneurial Skills
Time Management 385
Planning a Career in
Transportation 390
Winning Edge
BPA Small Business Management
Team Event 391

Glossary 392

Index 397

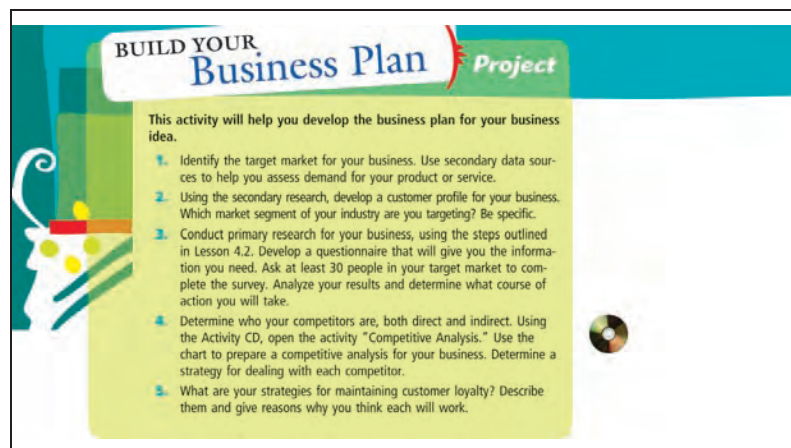


About the Author

Cynthia L. Greene taught business education at the high school level for 25 years. She taught in the Fulton County School System in Atlanta, Georgia, and she was the program specialist for Business and Information Technology for the Georgia Department of Education for six years. She has been active in the National Business Education Association (NBEA), serving as NBEA President in 2005–2006 and on the Entrepreneurship Standards Committee as a writer and reviewer and as a writer for the Entrepreneurship Lesson Plans.

Excellent Business Plan Coverage

Entrepreneurship: Ideas in Action takes you step-by-step through the entire process of owning and managing a business. Business plan coverage has been moved earlier in the text and expanded. You learn what it takes to get an entrepreneurial venture off to a good start.

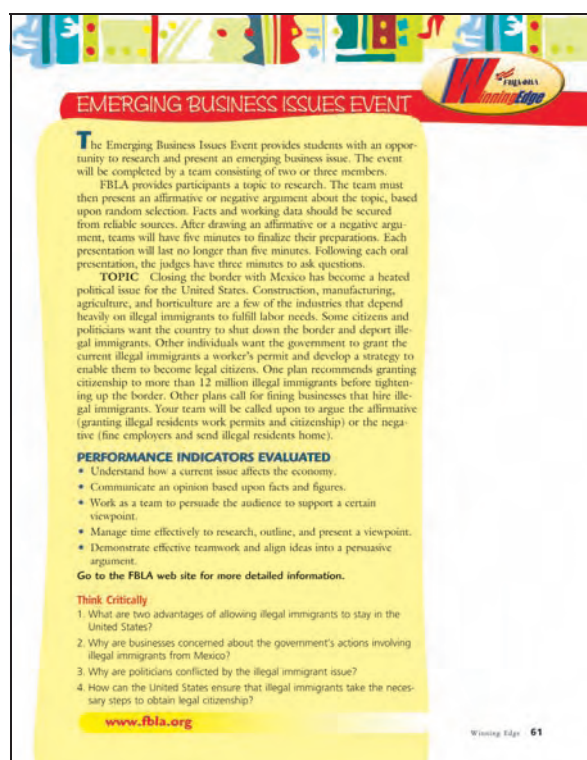


Build Your Business Plan Project concludes each chapter and is designed to help you prepare a complete business plan by the end of the course.

Comprehensive Coverage of BPA, FBLA, and DECA Competitive Events

Winning Edge features help you prepare for competitive events.

- BPA Presentation Management Team 33
- FBLA Emerging Business Issues Event 61
- BPA Prepared Speech 89
- FBLA Multimedia Presentation 117
- BPA Global Marketing Team Event 145
- DECA Entrepreneurship Promotion Project 175
- DECA Business Law and Ethics Management Team Decision Making Event 207
- DECA Buying and Merchandising Management Team Decision Making Event 235
- FBLA Business Financial Plan 267
- FBLA Partnership with Business 297
- FBLA Business Plan 329
- DECA Business Services Marketing Series Event 359
- BPA Small Business Management Team Event 391

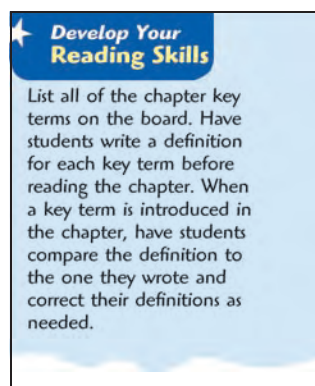


Excellent Organization!

Each chapter is organized into lessons, making the text easy to use in all classroom environments. Each lesson begins with a list of **terms** and **goals** for the lesson to help you focus your reading. Each goal corresponds to a major heading. Loaded with activities, individual and group projects, and reinforcement opportunities, this text will get you ready to launch your business ideas!

Lessons provide the appropriate amount of material for each lesson.

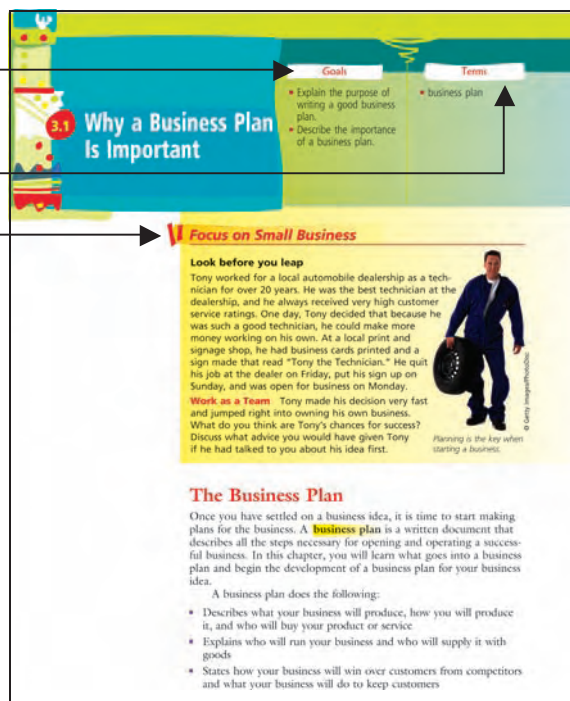
Develop Your Reading Skills helps hone your reading skills.



Goals outline the main objectives of the lesson.

Terms are the new terms defined in the lesson.

Focus on Small Business provides a motivating introduction to the lesson.



Career Coverage!

A variety of careers as an Entrepreneur are featured for various **Career Clusters** in the **Planning a Career in...** feature

Human Services 32
 Property Management 60
 Landscape Architecture 88
 Marketing Research 116
 E-marketing 144
 Public Safety 174
 Franchising 206
 Architecture and Construction 234
 Finance 266
 Information Technology 296
 Audio-Video Technology 328
 Insurance 358
 Transportation 390

**Planning a Career in
Architecture and Construction**



"My uncle is visiting from out West. He is excited about the solar panels he recently installed at his home. His city provided a \$1,000 rebate for solar panel installation. To obtain the rebate, the panels need to annually displace 1,500 kilowatt hours of grid-based power. My uncle's utility bills have gone down. He also feels good about doing his part to improve the environment by decreasing his dependence on the grid."

How do individuals and organizations transition their energy resources from traditional sources to environmentally friendly, renewable sources?

Solar power is a renewable energy source that is rapidly increasing in popularity. Many companies are available to guide individuals and corporations in utilizing solar energy and to assist in solar panel installation.

EMPLOYMENT OUTLOOK

- Solar energy consumption is expected to grow as part of the overall growth of U.S. energy consumption.
- Workers who are trained to participate in alternative energy sources may experience good job prospects.
- Individuals with college coursework in high-end technology will have the best opportunities in the utilities industry.

JOB TITLES

- Solar Installer
- Consultant, Solar Energy
- Solar Energy Project Manager
- Photovoltaic Lighting Designer
- Solar System Design Engineer

NEEDED SKILLS

- A Bachelor's Degree in Science, with an engineering major, is required for higher-level design, production, and management jobs.
- Expertise in a variety of areas including journeyman-level electrical knowledge, plumbing, and mount racking systems is needed for solar panel installers.

What's it like to work in Architecture and Construction? Paige, a solar panel installation contractor, has obtained installation contracts from a variety of companies. The companies that contracted for Paige's services provide their clients with on-site consulting, ranging from determining the optimal location of solar panels, to the filing of paperwork for government-based rebate and tax credit programs, to providing a six-month follow-up visit to ensure proper functioning of panels.

As Paige has been installing panels for many years, her experience is broad-based. Given the breadth of her experience, she can install panels at residential, commercial, or industrial sites.

Paige is planning to attend a conference that will focus on state and federal solar energy incentive programs. Becoming more knowledgeable about these issues is part of Paige's continuing education plan to prepare her to start her own solar energy consulting business.


What about you? Would you like to help clean up the environment by actively converting energy consumers to renewable, "green" energy sources?

234 Chapter 8 Launch and Set Up Your Business

Skills for Entrepreneurs!

Sharpen Your (Entrepreneurial, Teamwork, Leadership, Technology) Skills features offer skill-building information and pose critical-thinking questions.

Effective Business Letters 26
 Effective Presentation Skills 55
 Using Technology Tools 83
 Using Spreadsheets to Analyze Data 111
 Breakeven Point 139
 Marketing and the Web 169
 Effective Telephone Conversations 201
 E-Mail Etiquette 229
 Prepare a Resume 261
 Leadership Skills 291
 Promoting Teamwork 323
 Respect Cultural Diversity 353
 Time Management 385


Sharpen Your Entrepreneurial Skills

Respect Cultural Diversity

In today's global economy, you will come in contact with all kinds of people. Many of these people will be from cultures different from your own. You may work with people of different cultures. You may also buy from and sell to people of different cultures. As an entrepreneur, you need to appreciate different cultures for the following reasons:


- You need to be comfortable with your customers. If you are open to other cultures, you can attract more customers.
- People from different cultures may have different needs and wants. Understanding these can help you market your business more effectively.

How can you develop good relationships with everyone you do business with? There are at least five things you can do to enhance these relationships:

1. **Avoid stereotyping people.** Don't assume that all people from a particular ethnic or cultural group hold the same values and opinions, behave the same way, or like the same things.
2. **Focus on similarities rather than differences.** Most people, regardless of their culture, want the same things in life.
3. **Learn about different cultures.** Learning about a different culture will make you more comfortable around people from that culture. Learn how people in a different culture live and work.
4. **Make friends with someone from a different culture.** The friendship will help you begin to appreciate other cultures.
5. **Try to understand and identify with other people's feelings.** Try to see the world through the eyes of people from different cultures. Try to understand cultural views that are different from your own.

TRY IT OUT

Before conducting business in another country, you will have to answer many questions to address the risks. Will your product sell well in another country or will you have to make modifications to it? What aspects of the country's culture could affect your business? How can you learn about another country's culture? Using the Activity CD, open the activity "Competing in the Global Economy." Print a copy and complete the activity.



Sharpen Your Entrepreneurial Skills 353

Case Studies of Entrepreneurs!

Ideas in Action presents stories of successful young Entrepreneurs.

- Making Job Connections 3
- Michael Stahl, 4Teens Network
- Web Site Design 35
- Scott Smigler, Exclusive Concepts
- Turning an Idea into a Business 63
- Jeffrey Rodriguez and John Serrano, Latin Artist
- Serving Customers' Needs 91
- Brian Hendricks, StartUpPC and VB Solutions
- Turning Creative Fun into Dollars 119
- Sheri and Rich Schmelzer, Jibbitz
- Turning a Bad Experience into a Million Dollars 147
- Jasmine Lawrence, Eden Body Works
- Capitalize on Youth Marketing 177
- Tina Wells, The Buzz International Marketing Group
- A Neighborhood Business 209
- Ryan Williams, Rapappy
- Electronic Safekeeping 237
- Katelin Shea, GadgetSleeves
- Entertaining and Planning 269
- Andrew Jensen, Jx2 Productions



- Working for What You Believe In 299
- Omar Faruk, LogicLotus
- Growth is Risky 331
- Scott Alterman, The Icebox
- Starting Young and Moving Up 361
- Joseph Pascaretta, Alps Technology and Alps Lawn Company

Famous Entrepreneurs features successful entrepreneurs throughout history.

- Madam C. J. Walker 7
- Paul Revere 44
- Walter Elias Disney 67
- Thomas A. Edison 98
- Sergey Brin and Larry Page 122
- Anne Barge 167
- Eli Whitney 197
- Rachel Ray 221
- The Wright Brothers 243
- Ganz Family 281
- J. K. Rowling 312
- Merv Griffin 351
- Johnny Pag 383



Special Features Enhance Learning!

What Went Wrong? highlights the pitfalls of real entrepreneurs and includes critical thinking questions to help students analyze the situations.

Did You Know? offers additional information that relates to chapter topics.

WHAT WENT WRONG

Partnership Woes

Stan and Peter met while working at a video production company. Stan was in charge of editorial and production. Peter ran the sales force. Stan decided to begin his own company and invited Peter to join him. SP Communications seemed like a perfect partnership. Peter would handle sales and administration, while Stan managed clients and directed production. Things seemed to be going well until Peter decided he wanted to be a part of the creative process. He spent most of his time producing videos rather than looking for new business. Because of their friendship, Stan trusted that Peter was taking care of his side of the business.

As it turned out, Peter wasn't very good at the creative tasks he took on. He made mistakes that reduced expected profits. In addition, he wasn't making new sales contacts, which was supposed to be his main job.


By the time Stan realized what was happening to the business, it was too late. There weren't any new sales. What Stan thought

were profits were the result of Peter not paying their bills. Stan was left with more than \$150,000 in unpaid bills and other debts. Peter left the business. It took Stan three years to dig out of the financial mess and get his new company up and running successfully.

Think Critically

1. How might Stan and Peter have avoided the problems that led to the end of their partnership?
2. Why is this situation a good example of the difficulty in maintaining partnerships between friends?
3. What types of things should be spelled out completely between partners at the beginning of the partnership?

Choose your partners wisely.



did you KNOW?

According to a recent report by IGD, a consumer and shopper research company, 35% of shoppers visit only the aisles which they believe have the items they need. This indicates the importance of placing new products or promoted items in key locations to ensure good product exposure.

Be Your Own Boss gives you the opportunity to complete the same types of activities that a real entrepreneur might do.

BE YOUR OWN BOSS

You are the owner and manager of a diner located along a busy interstate highway. You do a good business with travelers passing through as well as locals who eat with you regularly. Recently, there have been several robberies during operating hours in nearby businesses. Your local customers are beginning to get a little nervous about coming to your business. Outline a plan to minimize your risk of robbery. Include ways to make your customers feel safe.

Net Bookmark incorporates Internet activities into every chapter.

NETBookmark

What makes a memorable brand or product name? Access school.cengage.com/entrepreneur/ideas and click on the link for Chapter 5. Author Phillip Davis provides some thoughts in his e-zine article. What does Davis consider the most common naming mistake? Do you agree with him that "Apple" is a better brand name than something like "United Computer Manufacturers" or "Quality Computer Corporation"? Why or why not? Provide one example of a product or business that you think has a great name, and another that you think has a poor name. Explain your answers.

school.cengage.com/entrepreneur/ideas

What Would You Do? ethics activities will help you think critically about ethical concepts.

WHAT WOULD YOU DO?

You asked two of your employees to work extra hours over the weekend to perform a physical inventory. You are certain that there were three plasma television sets in stock prior to having the employees take inventory. However, when the inventory was completed, the list showed only two plasma television sets in stock. You checked the stockroom, and you found only two. You have always trusted your employees. What would you do? Will you confront the employees? If so, how will you approach them? Working with a partner, role play the conversations you will have with the employees.

Ongoing Assessment!

Ongoing review and assessment help you understand the material.

Checkpoint enables you to test your understanding at key points in each lesson.

Lesson Assessment contains activities to help you apply what you have learned in the lesson.

Activities CD contains exercises that help you improve your entrepreneurial and economic skills.

Teamwork provides you with opportunities to work with classmates on cooperative learning projects.

Checkpoint
What are the six steps of market research?

4.2 Assessment

THINK ABOUT IT

- Why do entrepreneurs need to conduct market research?
- What are the limitations of market research?
- What is the difference between primary and secondary data?
- Why do you think short questionnaires are more effective than long ones?
- Why is it important to define the question you want your market research to answer?

MAKE ACADEMIC CONNECTIONS

- MANAGEMENT** Your family-owned business processes and sells orange juice to food distributors. In order to grow, the business needs to expand its product line. Apply the six market research steps to help determine an additional product for your business.
- COMMUNICATION** It is important to evaluate the effectiveness of a survey. Using the Activity CD, open the activity "Market Research Evaluation." Print a copy and complete the activity.

TEAMWORK

Working with team members, come up with a new product that you think will be very useful for students in your school. Develop a questionnaire for potential consumers of this product to gauge their interest. Have students from your school complete the questionnaire. Tabulate the results and determine if the product is a good idea.

Chapter Assessment provides a summary of the main points and contains questions and activities to test your knowledge.

Chapter 3 Assessment

SUMMARY

3.1 Why a Business Plan is Important

- A business plan is a written document that describes all the steps necessary for opening and operating a successful business. It explains the idea behind your business and spells out how your product or service will be produced and sold. It sets specific objectives and describes how your business will achieve them. It describes the backgrounds and experiences of the people who will be running the business.
- Writing a business plan is important because it makes you think about all aspects of your business, helps you secure financing for your business, helps you communicate your ideas to others, and can serve as a tool for managing your business.

3.2 What Goes into a Business Plan?

- The main body of the business plan should include the following sections: Introduction, Marketing, Financial Management, Operations, and Concluding Statement.
- To complete the business plan, you need to prepare introductory elements consisting of the cover letter, title page, table of contents, statement of purpose, and executive summary. The executive summary is the most important element and should not be written until the main body of the plan is complete. You also need to compile an appendix, which includes supporting documents that provide more information to the readers of the plan.

3.3 How to Create an Effective Business Plan

- To show you have a practical business idea, you must include information and data from objective sources. People from many organizations—including the SBA, the SBDC, SCORE, your local chamber of commerce, trade associations, professional business consultants, and financial institutions—can help you with your business plan. Print resources can be obtained at the public library and through Government agencies. An extensive amount of information is also available on the Internet.
- Common mistakes made in business planning include unrealistic financial projections, an undefined target market, poor research, ignored competition, and inconsistencies in the business plan.

Write a Question?
Read Ideas in Action on page 63 again. Then answer the questions a second time. How have your responses changed?

VOCABULARY BUILDER

Match each statement with the term that best defines it. Some terms may not be used.

- A written document that describes all the steps necessary for opening and operating a successful business.
- A financial statement based on projected revenues and expenses.
- A letter that introduces and explains an accompanying document or set of documents.
- A short restatement of a report.
- A brief explanation of why you are asking for a loan and what you plan to do with the money.
- An independent agency of the federal government created to help Americans start, build, and grow businesses.
- Organizations made up of professionals in a specific industry.
- Organization made up of more than 10,500 retired executives who volunteer their time to provide entrepreneurs with real-world advice and know-how.

- business plan
- cover letter
- executive summary
- gross family financial statement
- Service Corps of Retired Executives (SCORE)
- Small Business Administration (SBA)
- Small Business Development Centers (SBDC)
- statement of purpose
- trade associations

REVIEW YOUR KNOWLEDGE

- A business plan is not intended for
 - your competition
 - potential investors
 - your bank
 - any of the above
- Purposes of a business plan include which of the following?
 - it explains your idea for a product or service
 - it sets specific objectives and describes how they will be achieved
 - it describes the backgrounds and experiences of the people who will run the business
 - all of the above
- A business plan is important for a new business for all of the following reasons *except*
 - it makes you think about all aspects of your business
 - it can help you communicate your ideas to others
 - it guarantees you will get financing for your business
 - it can serve as a tool for managing your business
- The main body of a business plan includes which of the following elements?
 - executive summary
 - statement of purpose
 - financial management
 - supporting documents
- Which of the following is not a true statement regarding risk?
 - Identifying the possible risks your business faces will alarm lenders and investors and cause them to withhold funds.
 - Potential investors and lenders want to know what risks your business faces and how you plan to deal with them.
 - Lenders will appreciate the fact that you know what risks your business faces and have a plan for dealing with them.
 - Lenders know that every business faces risks.
- The purpose of including supporting documents in a business plan is to
 - make the plan lengthy
 - provide additional information
 - give the readers more information than they might need
 - explain your business idea
- Writing a business plan
 - is a quick and easy process
 - is quick but difficult
 - requires patience, research, thought, and time
 - none of the above
- Which of the following organizations can provide assistance when writing your business plan?
 - bank
 - Chamber of Commerce
 - Small Business Development Center
 - all of the above
- Which of the following describes why you are asking for a loan and what you plan to do with the money?
 - cover letter
 - statement of purpose
 - executive summary
 - title page
- Mistakes to avoid when preparing your business plan include all *except*
 - providing unrealistic financial projections
 - wasting time on research
 - ignoring the competition
 - failing to define the target market

APPLY WHAT YOU LEARNED

- Obtain a sample business plan. Review the business plan and discuss whether or not the five common mistakes in writing a business plan were avoided. Provide reasons to support your decisions.
- You plan to open a skateboarding park. What kind of research should you do? What sources will you consult for your research?

MAKE ACADEMIC CONNECTIONS

- COMMUNICATION** You are preparing a business plan for a self-storage facility (U-Store-It). You are requesting a \$75,000 loan to buy the property and storage lockers. Write the cover letter to the bank loan officer and a statement of purpose.
- RESEARCH** Choose a business with which you are familiar. Using the Activity CD, open the activity "Trade Association Research." Print a copy and complete the activity by using the Internet or the library to research trade associations that could provide useful information to the business.
- COMMUNICATION** An entrepreneur's resume is an important supporting document for a business plan. It tells the reader about the entrepreneur's qualifications for running the business. Research resume formats and choose one that you think would be suitable for you. Prepare a resume outlining your experience for running a business.

Chapter 1



© Digital Vision

Should You Become an Entrepreneur?

1.1 All about Entrepreneurship

1.2 Is Entrepreneurship Right for You?

1.3 Exploring Ideas and Opportunities

1.4 Problem Solving for Entrepreneurs

school.cengage.com/entrepreneur/ideas

IDEAS IN ACTION

Making Job Connections

The foundation of the U.S. economy is entrepreneurship. Today's large corporations were yesterday's small businesses. Identifying a need and coming up with a product or service to meet it are what entrepreneurship is all about. Some famous entrepreneurs in history include Levi Strauss and Olive Ann Beech. More recent entrepreneurs include Bill Gates and Oprah Winfrey. You or someone you know could be a future successful entrepreneur. Prepare yourself to turn ideas into action and seize the opportunity when it comes!



Michael Stahl, 4Teens Network, LLC

© Courtesy of Michael Stahl

As a chapter president of Future Business Leaders of America (FBLA), Mike Stahl came across an idea for a business while coordinating a job fair for the Blue Valley School District in Kansas City, Missouri. He heard fellow students complain about not knowing where to look for jobs, and he heard employers express a need for qualified help. This inspired Mike to come up with the idea for 4Teens Network, LLC, which he ran with his partner, Ephren Taylor, Jr. Through an interactive web site featuring employer advertisements and registered job seekers, 4Teens Network matched employers and employees.

Seeing the potential of this opportunity, Mike and Ephren tested the business model before seeking outside financing. Their testing included various web site designs, sales and marketing plans, and pricing structures. In the first five months of testing, the company returned 300 percent on its initial investment. This gain showed Mike, Ephren, and potential investors that this venture had great possibilities. The time and energy spent in planning and testing their business model helped prepare 4Teens Network, LLC, for a successful future.

The web site asked job seekers a set of questions and used answers to build a professional resume, which could be sent to job listings on the site. Users get an e-mail account to receive e-mail replies from prospective employers.

Mike and Ephren plan to build their business across the United States and even internationally, but they aren't losing sight of their original mission—to provide a service for their community.

What do you know?

1. Who do you think was one of the most important entrepreneurs of the past?
2. Who do you think is one of the most important entrepreneurs of the twenty-first century?
3. Can you identify a need in your school or community that might be met by the creation of a new business?

1.1

All about Entrepreneurship

Goals

- Define entrepreneurship.
- Recognize the role entrepreneurs play in the U.S. economy.
- Examine the reasons that businesses succeed or fail.

Terms

- entrepreneurs
- entrepreneurship
- employees

Focus on Small Business

Should you be your own boss?

"I'm so tired of someone telling me what to do all the time," Delia said to her friend Gloria. "I know what you mean," Gloria answered, "because I get the same thing." "It seems like there should be some way we could be in charge," Delia said. "There's got to be a better way. I've got an idea," Gloria said, "let's be entrepreneurs." "Entrepe... what?" questioned Delia. "Entrepreneurs," Gloria answered. "Mr. Riviera talked about them in my business class last week. They are people who start and run their own businesses. We could do that!"

"What would we have to do? Would we make a lot of money? Would it be fun? Would we get to do whatever we wanted?" Delia's mind was overflowing with questions. Gloria was getting very excited as she replied, "We could be our own bosses! If we were the owners, we would be in charge! We'd get to make all the decisions!" "This is starting to sound pretty good," Delia replied as she began to share Gloria's excitement. "We could decide when we work, what we do, and how we do it. And, we can make lots of money! I can't wait. When do we start?"

Work as a Team Many people go into business just so they can be in charge and make lots of money. Do you think this is the most important reason to start your own business?



© Rubberball Productions

Start-up companies stay alive with new technology.

What Is an Entrepreneur?

The U.S. economy includes thousands of small businesses. Many of these small businesses are owned and operated by men and women who created their own companies. Some of these individuals have become legends as you hear stories about their paths to success. But what makes someone an entrepreneur? What impact have entrepreneurs had in history? What impact do they have today?

People who own, operate, and take the risk of a business venture are called **entrepreneurs**. They are engaged in **entrepreneurship**, the process of running a business of one's own. Entrepreneurs come from all types of backgrounds and create all kinds of businesses. People of all ages choose to become entrepreneurs. Some own tiny craft shops, while others own huge construction companies. Entrepreneurs try to identify unmet needs in the marketplace. Then they provide a service or product to meet those needs. When they succeed, their businesses flourish, and profits are earned. But if their business idea is unsuccessful, they may lose the money invested in their business.

EMPLOYEES VS. ENTREPRENEURS Entrepreneurs assume risk. This makes them different from **employees**, who are people who work for someone else. Both may make decisions, but only the entrepreneur is directly affected by the consequences of those decisions. Sam Jones manages a record store owned by Felipe Santiago. Sam decides to keep the store open until midnight during the week. If the additional hours bring in customers and increase profits, Sam may be praised by Felipe. He may even get a raise. However, Sam won't directly receive any of the profits because he is an employee. The additional earnings will flow to Felipe, the owner.

WHY DO PEOPLE BECOME ENTREPRENEURS? People go into business for themselves for many reasons. Some want to leave the fast-paced corporate environment and set their own schedules. Others want to be at home but still earn an income. Still others want to pursue a personal dream. You might choose to become an entrepreneur for completely different reasons.

Types of Entrepreneurial Businesses

There are generally four types of businesses, and there are opportunities for entrepreneurs in each type. See the chart on page 6. *Manufacturing businesses* actually produce the products they sell. Using resources and supplies, they create everything from automobiles to paper. *Wholesaling businesses* sell products to other businesses rather than the final consumer. For example, a wholesaler supplies your local greeting card store with items such as cards and wrapping paper. *Retailing businesses*, such as a greeting card store, sell products directly to those who use or consume them. *Service businesses* sell services rather than products. They include hotels, hairdressers, and repair shops.

OTHER BUSINESS AREAS Two other categories of businesses are (1) agricultural and (2) mining and extracting businesses. *Agricultural businesses* generate fresh produce and other farm products, such as wheat. *Mining and extracting businesses* take resources like coal out of the ground so they can be consumed.

Checkpoint

Describe different types of entrepreneurial businesses.

Develop Your Reading Skills

As you read this chapter, write down questions related to headings and photos. Share your questions with the class.



TYPES OF BUSINESSES			
Manufacturing	Wholesaling	Retailing	Service
Apparel and other textile products Chemicals and related products Electronics and other electrical equipment Fabricated metal products Food products Industrial machinery and equipment Printing and publishing Rubber and miscellaneous plastic products Stone, clay, and glass products	Apparel Electrical goods Groceries and related products Hardware, plumbing, and heating equipment Lumber and construction materials Machinery, equipment, and supplies Motor vehicles and automotive equipment Paper and paper products Petroleum and petroleum products	Auto and home supply stores Building materials and supply stores Clothing stores Florists Furniture stores Gift, novelty, and souvenir stores Grocery stores Hardware stores Jewelry stores Retail bakeries Shoe stores Sporting goods and bicycle stores	Appliance repair Automotive repair Babysitting Bookkeeping Consulting Dance instruction Electrical services Exterminators Flower decorating House cleaning Lawn care Painting Plumbing Translating Travel agency Tutoring

Source: Small Business Administration

Recognizing Opportunity

Many of America's most successful companies started with one person who recognized an opportunity and came up with an idea for a business in response to that opportunity. Entrepreneurs have played an important role in the history of America's economy and will continue to shape our economy in the future.

According to estimates from the U.S. Small Business Administration's Office of Advocacy, there were approximately 25.8 million businesses in the United States in 2005. Recent census data show that there were 5.8 million firms with employees and 18.6 million without employees. Small firms with fewer than 500 employees represent 99.9 percent of the 25.8 million businesses in the United States. Only 17,000 U.S. businesses are considered large. Small businesses contribute billions of dollars to the U.S. economy every year and employ more workers than all of the country's large corporations combined. These small businesses are found in virtually every sector of the economy.

Small companies can be more creative and take more risks than large companies. Their experimentation and innovation lead to technological change and increased productivity. This makes small business a significant part of the American economy.

Entrepreneurs Who Changed America

Entrepreneurs change American business decade after decade. They establish new companies and fill unmet needs. They constantly change how things are done and contribute to the overall good of the nation. There are many businesses today that started small and have grown into large companies that are making a major impact in our economic system.



STARBUCKS COFFEE COMPANY Starbucks Coffee Company was founded in 1971, opening its first location in Seattle's Pike Place Market. Starbucks is named after the first mate in Herman Melville's novel *Moby Dick*. It is the world's leading brand of specialty coffee. Its stores receive more than 40 million customer visits per week at coffeehouses in North America, Europe, the Middle East, Latin America and the Pacific Rim. When Howard Schultz first joined the company in the early 1980s, Starbucks was already a highly respected local roaster and retailer of whole bean and ground coffees. A business trip to Italy, where he was impressed with the popularity of espresso bars in Milan, helped Schultz recognize an opportunity to develop a similar coffeehouse culture in Seattle. Espresso drinks became an essential element of Schultz's vision. He purchased Starbucks with the support of local investors in 1987. In addition to its well-situated coffeehouses, Starbucks markets its coffee and tea products through its web site and through many national retail supermarkets.

THE HOME DEPOT In 1979, Bernie Marcus and Arthur Blank opened the first The Home Depot stores in Atlanta, Georgia, forever changing the home improvement industry. The original stores stocked around 25,000 products. An average store today offers 40,000 products in approximately 105,000 square feet. Marcus and Blank's vision was of warehouse stores filled from floor to ceiling with a wide assortment of home improvement products at the lowest possible prices and with the best possible service. Within five years, The Home

Famous Entrepreneur

Madam C. J. Walker

You may have heard it said that "necessity is the mother of invention." Many entrepreneurs got their start by creating something that they themselves needed and then sharing their product with others. That's exactly what made Madam C. J. Walker a millionaire. Walker, originally known as Sarah Breedlove, suffered from a scalp ailment during the 1890s and began experimenting with homemade remedies. Her remedies worked well, so she began offering them to other African-American women. In 1905, she moved to Denver, married newspaperman Charles Joseph Walker, and started her own company. She sold her products door to door and bought ad space in newspapers.

Walker later opened Lelia College, where she and her daughter trained other women to use and sell the product line, which had expanded to include items such as complexion soap and dental cream. At least 20 women completed the program every six weeks. Besides becoming a millionaire from the sales of her products, Walker made a huge contribution to the African-American community by empowering women to make their own mark in the business world.

Think Critically

Why is it important for entrepreneurs to make contributions to their community in addition to offering a product or service?



© A'Lelia Bundles/Walker Family Collection/madamcjwalker.com

Why do you think Madam C. J. Walker became such a successful entrepreneur?

Depot expanded from Georgia to Florida, Louisiana, Texas, and Alabama. Today, it has more than 2,100 stores throughout the United States, Canada, and Mexico. The company also runs EXPO Design Centers and The Home Depot Supply wholesale stores.

HARPO PRODUCTIONS, INC. Oprah Winfrey's love of acting and her desire to bring quality entertainment projects into production prompted her to form her own production company, HARPO Productions, Inc., in 1986. Today, HARPO is a formidable force in film and television production. Based in Chicago, HARPO Entertainment Group includes HARPO Productions, Inc., HARPO Films, and HARPO Video, Inc. In October 1988, HARPO Productions, Inc. acquired ownership and all production responsibilities for *The Oprah Winfrey Show* from Capitol Cities/ABC, making Oprah Winfrey the first woman in history to own and produce her own talk show. The following year, HARPO produced its first television miniseries, *The Women of Brewster Place*, with Oprah Winfrey as star and executive producer. Oprah also produced and appeared in the made-for-television movies *There Are No Children Here* (1993) and *Before Women Had Wings* (1997). In 1998, she starred in the feature film *Beloved*, based on the book by Nobel Prize-winning American author Toni Morrison.

Checkpoint

Describe how one of the entrepreneurs discussed above recognized an opportunity to develop a successful business.



Why do you think some people choose to start their own business?

Business Success or Failure

According to a recent study by the Small Business Administration's Office of Advocacy, two-thirds of new businesses survive at least two years, and 44 percent survive at least four years. This means that over half of all new businesses do not survive beyond four years. These results are similar for different industries. Many people think that there is a higher failure rate for restaurants than other types of businesses. However, leisure and hospitality establishments, which include restaurants, survive at rates only slightly below the average. Major factors in a firm's success include having adequate capital, providing a product or service that meets customer needs, the owner's education level, and the owner's reason for starting the firm in the first place, such as freedom for family life or wanting to be one's own boss. The reason must sufficiently motivate the entrepreneur to have the perseverance to succeed.

The owner's business experience is a factor that contributes to the likelihood of success. Experienced businesspeople have an understanding

of how to purchase products and services. They know how to plan, negotiate with suppliers, raise money, negotiate leases, sell and market their product or service, and manage finances. Many businesses fail because the owner lacks business knowledge. Someone may have an idea for a product or service but lack the necessary business skills he or she needs to run a successful business. There is a major difference in having expertise regarding a product or service and running a business with that product or service.

Checkpoint

What factors contribute in helping a business to succeed?

1.1 Assessment

THINK ABOUT IT

1. What are your reasons for wanting to become an entrepreneur? Do you think they are common to all entrepreneurs, or are some of your reasons unique?
2. Why do you think entrepreneurship is important to the U.S. economy? Provide specific examples of how entrepreneurs affect the economy.
3. What do you think is the most important thing an entrepreneur should do before starting a business?

MAKE ACADEMIC CONNECTIONS

4. **MATH** Suppose there are exactly 5,812,000 small businesses in the economy today. Approximately 27 percent of those businesses are service businesses. What is the number of service businesses in the economy?
5. **SOCIAL STUDIES** Before Starbucks grew nationwide, there were few places that people could go to have coffee and meet with friends and business associates. Write at least one paragraph about how Starbucks and other coffee shops have changed the way people view coffee and its role in society.
6. **COMMUNICATION** Entrepreneurs can be of any age. Research a teen entrepreneur. Write a one-page paper about his or her business. Discuss whether or not you think the business idea is a good one. Make recommendations for expanding the business.



TEAMWORK

Gather in teams. List advantages and disadvantages of being an employee. List advantages and disadvantages of being an entrepreneur. Compare and contrast the lists.



1.2

Is Entrepreneurship Right for You?

Goals

- Identify the characteristics of successful entrepreneurs.
- Identify the characteristics of good team members.
- Assess whether you have what it takes to succeed in your own business.

Terms

- self-assessment
- aptitude

Focus on Small Business

Think it through!

Gloria and Delia were excited about starting their own business, but as they continued their discussions, Gloria realized they needed to slow down and think through the process carefully. "You know, Delia, it's not really easy to start our own business. When we talked about this in class, Mr. Riviera said that there are a lot of things to consider before starting a business. First, we need to decide what we like to do and what we are good at. Then we have to do a lot of research and planning if we want to be successful."

Thinking about what Mr. Riviera told her in class, Delia sighed. "This entrepreneur thing sounds like a lot of work. What do you think we should do?"

Work as a Team Many people go into business without first taking time to examine their strengths and weaknesses and what they really like to do. Do you think it's a good idea for Gloria and Delia to slow down and really examine their interests before starting the business?



Examine your strengths and weaknesses before starting a business.

© Dorling Kindersley/Getty Images

Characteristics of Successful Entrepreneurs

Many people dream of running their own businesses. They would like to become entrepreneurs. Entrepreneurship can be exciting, but many go into it not realizing how difficult it is to run their own business. In fact, statistics show that most new businesses will fail within a few years. These startup businesses fail because of the owner's poor planning, lack of business knowledge, lack of entrepreneurial characteristics, inability to work with others, or failure to choose the right business.

Researchers have identified several characteristics that distinguish successful entrepreneurs from those that fail.

1. **Successful entrepreneurs are independent.** They want to make their own decisions and do something they enjoy.
2. **Successful entrepreneurs are self-confident.** Entrepreneurs make all the decisions. They must have the confidence to make choices alone and bounce back from a poorly made decision.
3. **Successful entrepreneurs have determination and perseverance.** Entrepreneurs persist through hard times until goals are met.
4. **Successful entrepreneurs are goal-oriented.** They know what they want, and they are able to focus on achieving it.
5. **Successful entrepreneurs have a need to achieve and to set high standards for themselves.** They are motivated by setting and achieving challenging goals.
6. **Successful entrepreneurs are creative.** They think of new ways to market their businesses and are always looking for new solutions to problems.
7. **Successful entrepreneurs are able to act quickly.** They are not afraid to make quick decisions when necessary, which helps them beat their competitors.
8. **Successful entrepreneurs keep up to date with technology.** New technologies emerge that can help with many business activities. In order to run their business efficiently, entrepreneurs should always be on the lookout for new technology they can apply to their business.

did you KNOW?

According to the Center for Women's Business Research, as of 2006, nearly 10.4 million firms were owned by women. These firms employed more than 12.8 million people and produced \$1.9 trillion in sales.



© Getty Images/PhotoDisc

Why would it be important for the owner of an auto repair shop to keep up to date on the latest technology?



Ryan Nelson has many entrepreneurial characteristics. Since he was 14, Ryan played for his high school basketball team. Other boys his height—just 5'8"—would not have enjoyed competing with much taller boys. Ryan accepted that he would have to work harder to win. He needed to be creative in handling the ball. Most of all, he had to believe in himself. He did, and he became one of the top players on his team. If Ryan opened his own business, the characteristics he displayed as a ball player might help him succeed.

Checkpoint

Name three important characteristics of entrepreneurs.

Characteristics of Good Team Members



© Getty Images/PhotoDisc

How can participation on a sports team help prepare you to become an entrepreneur?

Entrepreneurs realize that there are other stakeholders in their businesses—partners, investors, employees, suppliers, customers, creditors, and so forth. They must work with others to get their business up and running. They must have good team-building skills as well as be effective team members. Good team members display the following traits:

1. **Commitment** They are committed to team goals and willing to work hard to achieve the goals.
2. **Competency** They have the right set of skills needed to get the job done and to help accomplish the team's goals.
3. **Communication** They have good communication skills and can share ideas with others in both oral and written form.
4. **Cooperation** They must work well with others and know that they will not always get their way. They are willing to accept the decision of the group for the good of the group.
5. **Creativity** They are able to look at things from different perspectives and suggest new ways of doing things.

Ryan Nelson displayed these traits as a member of his basketball team. His experience will help him work effectively as part of a team in the business world. If Ryan becomes an entrepreneur, he could apply these skills when working with other people who will be important to his success.

Checkpoint

Why is it important for entrepreneurs to be good team members?

Are You Right for Entrepreneurship?

Entrepreneurship is not for everyone. Some people lack the qualities needed to become successful entrepreneurs. Others lack the aptitude needed to run a business. To determine if entrepreneurship is right for you, you first need to perform a self-assessment. A **self-assessment** is an evaluation of your strengths and weaknesses. You can do this in a number of ways. You can list what you believe to be your strengths and weaknesses on a sheet of paper. You can ask others what they believe your strengths are and where your weaknesses lie. There are also professional tests you can take to assess your abilities.

Assess Your Interests

Success as an entrepreneur requires a strong commitment to a business and a lot of energy. To be able to commit yourself fully to a business, you should choose a field that interests you and that will provide you with an experience you will enjoy. Many entrepreneurs

WHAT WENT WRONG



Experience Needed

Louise was a theatre performer who sang and danced in Broadway-style musicals. The work was not always steady, so she earned additional money working part time at a print shop. The elderly couple who owned the shop allowed Louise to work flexible hours so she could pursue a music career. Sadly, the husband died, and the wife decided to sell the business and move away. Louise was excited about the opportunity to purchase the business.

The former owner helped Louise gather financial information and put together a business plan. Louise's uncle cosigned a bank loan, and she was in business. She modernized the décor of the shop. Louise contacted all the existing customers to assure equal or better service. Sales increased the first two months. But then . . .

The former owner left town earlier than planned. Then Louise's chief printer quit. Using part-time employees, Louise was frantically trying to get large orders out on time. With no formal business training and no management experience, Louise couldn't begin to deal with all these problems—problems that even an experienced businessperson would find difficult. She ended up selling the business at a \$50,000 loss.

Think Critically

1. What characteristics did Louise possess that led her to become an entrepreneur?
2. What circumstances out of Louise's control led to the failure of this business?
3. What steps could Louise have taken to try to save her business?



© Digital Vision

Get some business training before starting a business.



center a business on an interest or hobby. Analyzing past experiences and jobs can also help. Building a business around jobs or experiences that you found fulfilling could lead to success.

Assess Your Aptitude

Different jobs require different job aptitudes. **Aptitude** is the ability to learn a particular kind of job. Auto mechanics must possess an aptitude for solving mechanical problems. They must also be good with their hands. People who sell insurance must have good interpersonal skills. Answering questions like those in the Job Attributes Checklist can help you identify the kinds of entrepreneurial opportunities that might match your aptitudes and interests.

Job Attributes Checklist

- ☐ 1. *I enjoy working with numbers.*
- ☐ 2. *I enjoy working outdoors.*
- ☐ 3. *I enjoy working with my hands.*
- ☐ 4. *I enjoy selling.*
- ☐ 5. *I like working with people.*
- ☐ 6. *I prefer to work alone.*
- ☐ 7. *I like supervising other people.*
- ☐ 8. *I like knowing exactly what it is I am supposed to do.*

Assess the Advantages of Entrepreneurship

Many people see significant advantages in owning their own businesses. Some of the biggest advantages include the following:

1. **Entrepreneurs are their own bosses.** Nobody tells an entrepreneur what to do. Entrepreneurs control their own destinies.
2. **Entrepreneurs can choose a business that interests them.** Entrepreneurs work in fields that interest them. Many combine hobbies and interests with business.
3. **Entrepreneurs can be creative.** Entrepreneurs are always implementing creative ideas they think of themselves.
4. **Entrepreneurs can make large sums of money.** Entrepreneurship involves risk, but if the business is successful, the business owner will reap the profits.

Assess the Disadvantages of Entrepreneurship

All prospective entrepreneurs must carefully weigh the advantages against the disadvantages before making the decision to start a business. Disadvantages include the following:

1. **Entrepreneurship is risky.** There is the possibility of losing money and going out of business.



2. **Entrepreneurs face uncertain and irregular incomes.** Entrepreneurs may make money one month and lose money the next.
3. **Entrepreneurs work long hours.** Entrepreneurs are never really finished with their jobs. They can work long, irregular hours. They receive no paid days off and often work evenings and weekends.
4. **Entrepreneurs must make all decisions by themselves.** Unless they have partners, entrepreneurs have the final responsibility for all decisions that are made regarding the business.

Checkpoint

What characteristics do you have that are best suited to entrepreneurship?

1.2 Assessment

THINK ABOUT IT

1. Entrepreneurs can fail even if they are committed and have the characteristics needed to be successful. How can this happen?
2. What traits do good team members have?
3. Do you think the advantages of entrepreneurship outweigh the disadvantages? Why or why not?

MAKE ACADEMIC CONNECTIONS

4. **MATH** One in three small companies begun this year will be out of business within the next two years. What percentage is this? Four years from now, only 44 percent of all businesses started will survive. Out of 90 new businesses, approximately how many will still be open in four years?
5. **CAREER SUCCESS** Choose a business idea that you think you would like. Using the Activity CD, open the activity "Job Attributes Checklist." Print a copy and complete the activity. Compare your interests to your business idea. Is this a good choice for you? Why or why not?



TEAMWORK

Work in teams to choose a successful entrepreneur. List the traits and aptitudes this person has that have contributed to his or her success. Develop a presentation about the entrepreneur to give to the class.



1.3

Exploring Ideas and Opportunities

Goals

- Identify sources for new business ideas.
- Recognize different business opportunities.
- Identify your own personal goals.

Terms

- opportunities
- ideas
- trade shows

Focus on Small Business

Find an idea

Gloria and Delia realized that although there are many advantages of owning your own business, there are many responsibilities and challenges that a business owner has to face. Gloria knew that she and Delia had their work cut out for them, but she had confidence they could do it if they put their minds to it. They also knew that before they started, they really needed to have a good idea and be sure that there were people who were willing to pay them for the product or service they wanted to sell.

"How do we decide what kind of business we should have?" Delia asked Gloria.

"There are so many businesses in our community," Gloria responded. "We've got to come up with just the right idea!"

Work as a Team How do people come up with ideas for new businesses? How do you think they decide if the idea is worth pursuing?



© Stockbyte

Spend time determining a good idea for your business.

Look for Ideas

Millions of entrepreneurs in the United States start their own businesses. You may wonder how they decided what businesses to operate. They may have acted on a new idea or an opportunity. An idea is different from an opportunity. **Opportunities** are possibilities that arise from existing conditions. **Ideas** are thoughts or concepts that come from creative thinking. Ideas can come from many different sources.

HOBBIES AND INTERESTS Many people get business ideas from their hobbies or interests. Bill had always enjoyed working with his

grandfather on the farm and had helped to build and maintain many farm structures. He built a garage and added a sunroom to his own home. He also was able to make plumbing, electrical, and carpentry repairs around the house. He started doing this for others in his spare time. Soon he had so many people calling on him for these services that he decided to start a general contracting business. Making a list of hobbies and interests can help you decide what business is right for you.

PAST EXPERIENCES Analyzing past experiences and jobs can help you come up with ideas for a business you would enjoy owning. People who excel at their jobs have generally learned much about their profession and how to satisfy customer needs. They also see how successful marketing is conducted. Through their work, they can build a network of potential customers, suppliers, employees, and distributors. When they feel confident that they can offer a product or service to this market more effectively than their current employer, they can start a new business.

Samantha Rodriguez worked as a computer network administrator for a large company. Recognizing that she could perform the same computer services for other companies, Sam started her own computer consulting service. She currently earns less money than she did working for a large company, but she enjoys working flexible hours and meeting new people.

DISCOVERY OR INVENTION Sometimes a business opportunity arises from a discovery or invention. Someone may invent a new tool that works better than tools that are currently available. The next step would be to research and find out if the idea can be patented, who the competition is, what the manufacturing process would be, and who the target market is.

David enjoyed working in his garden, but he did not like any of the tools he had for removing weeds from around the plants. He took one of his tools and made modifications to it and found that it worked perfectly. After several friends tried out the tool and liked it, David decided to investigate obtaining a patent for it.

NETBookmark

Many of America's most successful companies started with one person who recognized an opportunity and came up with an idea for a business in response to that opportunity. One of those people was Bill Gates, chairman of Microsoft, the largest software company in the world. Believe it or not, there was a day when even Microsoft was a small business. Access school.cengage.com/entrepreneur/ideas and click on the link for Net Bookmark Chapter 1. Read the article "A Little Company Called Microsoft." When and where was Microsoft founded? Who was Bill Gates' original business partner?

school.cengage.com/entrepreneur/ideas

Checkpoint

Where do new ideas for businesses come from?

Investigate Opportunities

People often do research to determine what is missing in a particular market—what needs exist that are not being met. By conducting this research, they hope to find the perfect business opportunity.

The Internet and the library have resources that can help you examine different opportunities. These include books on entrepreneurship, magazines for entrepreneurs, trade magazines for certain businesses, and government publications. *County Business Patterns* is an annual series of publications providing economic profiles of counties, states, and the country as a whole. Data include employment, payroll, and the number of establishments by industry.

This is not the only place to investigate opportunities. The Small Business Administration (SBA) is an organization that exists to help small businesses and their owners. It publishes information that may be helpful. Talking to entrepreneurs and attending **trade shows**, which are special meetings where companies of the same or related industry display their products, can also be beneficial.

Luanda Williams wanted to use her love of sports and dancing to create her own company. She found books and magazine articles at the library that gave her information on various kinds of businesses. She also talked to owners of gymnastic centers, health clubs, and dance studios. She discovered that there were not enough children's fitness programs to meet the demand in her area. All of the existing children's programs had long waiting lists. Her research revealed the many opportunities available in the children's fitness industry.

Compare Different Opportunities

Once you find appealing business opportunities, you need to identify which ones have the best chance for success. Now is the time to assess each business opportunity by asking yourself the following questions:

1. Is there a market in my community for this kind of business? Will people buy my product or service?
2. How much money would it take to start this business? Will I be able to borrow that much money?
3. How many hours a week is it likely to take to run this business? Am I willing to commit that much time?
4. What are the particular risks associated with this business? What is the rate of business failure?
5. Does my background prepare me to run this kind of business? Do most people who own this kind of business have more experience than I do?
6. How much money could I make running this business?

Checkpoint

How can you find out about various business opportunities?

Setting Goals

For everything you do in life, you set goals. Goals help you stay on track and follow through with your plans. The best goals are SMART. Smart goals provide more direction as shown below.

SMART GOALS	
Specific	Goals should be specific and answer "What?" "Why?" and "How?"
Measurable	Goals should establish ways to measure your progress
Attainable	Goals should not be too far out of reach
Realistic	Goals should represent things to which you are willing to commit
Timely	Goals should have a timeframe for achievement
Goal	I will learn more about starting my own business.
SMART Goal	I will learn more about starting my own catering business by obtaining information from the Small Business Administration and talking with the owners of three local catering businesses by the end of the month.



© PhotoDisc/Getty Images

As an entrepreneur, you will need to set many goals. Goals can be categorized as financial and nonfinancial.

FINANCIAL GOALS Set specific financial goals before starting a business. Financial goals can include how much money you will earn and how quickly you will pay off debts. Make sure your goals are realistic. If one of your goals is to make large sums of money early on, you almost certainly will be disappointed. It usually takes time for businesses to become well established and profitable. This means that, at first, an entrepreneur may earn less than he or she would have earned working as an employee.

Goals should be measurable and easily attainable in the time allotted. Mo Yang wants to start a mail-order business for model trains, planes, and cars. His income goal is to earn \$27,000 at the end of the first year. He estimates that after expenses he will earn \$9 for each item he sells. At this rate of profit, he would have to sell 3,000 models to meet his income goal. Mo realizes that this is not realistic. He would have to lower his income goal or find another business idea.

NONFINANCIAL GOALS Most people who own their own businesses do so for more than just monetary gain. They are looking for personal satisfaction. They may serve a community need, do something they like, or enjoy the personal independence of being an entrepreneur. You will want to specify what nonfinancial goals you want to achieve by being an entrepreneur. Setting and meeting nonfinancial goals can help

BE YOUR OWN BOSS

You are interested in starting your own business, but you are not sure what kind of business it should be. To help you get started, think about something you do that you really enjoy. Now think about ways that you might be able to turn this activity into a business. Make a list of businesses in your area that offer a related product or service. Write a paragraph explaining your business idea. How will your business be different from the existing businesses you listed?



an entrepreneur live a more satisfying and fulfilling life. Entrepreneurship can benefit many aspects of life.

Checkpoint

Why are financial goals important? Name some nonfinancial goals an entrepreneur may have.

1.3 Assessment

THINK ABOUT IT

1. Think about a business opportunity that appeals to you. For this business, answer the six assessment questions listed in this lesson on a sheet of paper. Is this a realistic choice for you? Why or why not?
2. In terms of annual income, what financial goals have you set for yourself for five years after you graduate? What nonfinancial goals have you set that you might be able to fulfill by becoming an entrepreneur? Are financial or nonfinancial goals more important to you? Why?
3. Your friend has set the following goal: I plan to eat healthier. Is this a SMART goal? Explain why or why not. What suggestions would you make for improving it?

MAKE ACADEMIC CONNECTIONS

4. **MATH** You live near the beach and have a passion for snorkeling. Your dream is to give snorkeling lessons. You estimate that after expenses, you can earn an average of \$10 per lesson. Each lesson will be one hour long, and you plan to offer lessons five days a week. Your income goal is \$15,000 per year. How many lessons do you need to give to achieve this goal? Is this goal realistic?
5. **COMMUNICATION** Write a letter to the Small Business Administration. In your letter, indicate your interest in starting a small business. Be specific about the type of business you wish to start. Ask what specific services the SBA provides to people who wish to start this type of business. Give your letter to your teacher.
6. **SOCIAL STUDIES** Write a personal nonfinancial goal involving your local community that you would like to achieve through entrepreneurship. Be sure the goal is SMART. Write an outline for a detailed plan you can follow to achieve this goal. Explain how it would benefit your community.



TEAMWORK

Working with classmates who have similar interests, come up with an idea for a business. Brainstorm a list of resources for finding information about similar businesses.

1.4

Problem Solving for Entrepreneurs

Goals

- List the six steps of the problem-solving model.
- Describe ways to improve your problem-solving skills.

Terms

- brainstorming

Focus on Small Business

Research your ideas

Gloria and Delia spent time on the Internet and in the local library researching ideas for their new business. As a result, they had come up with several ideas. Now they had to decide what to do with these ideas.

As they discussed their options, Gloria said, "You know, Delia, we can talk about these ideas, but we really need a system that we can use for solving problems. We want to be sure that we make the very best decisions for our business."

"Yes," Delia responded, "You are right. I remember reading about a problem-solving model in one of the books we found at the library. Let's go back and find it and see if we can adapt it for our use!"

Work as a Team How important do you think it is to use a system for solving problems?



© Digital Vision

Research will help you examine opportunities.

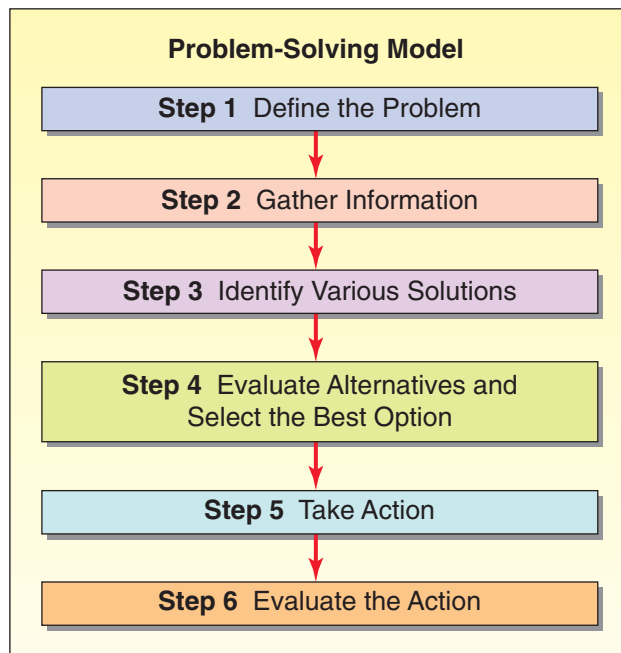
Use the Problem-Solving Process

As an entrepreneur, you will be faced with making decisions and solving problems every day. Whether or not to become an entrepreneur is a big decision. Many entrepreneurs make decisions casually or base them on intuition. As a result, their decisions are based on faulty assumptions or illogical thinking. The best entrepreneurs use formal problem-solving models to gather information and evaluate different options.

A formal problem-solving model helps people solve problems in a logical manner. The model consists of six steps: define the problem, gather information, identify various solutions, evaluate the alternatives and select the best option, take action, and evaluate the action taken.

Step 1 Define the Problem

Before you can solve a problem, you need to diagnose it. Write down what the problem is and why it is a problem. Try to quantify it too.



For example, you may be trying to decide whether to start your own business or work for another company. If you accept the job offer, your income would be \$30,000 a year. If you reject the job offer, you would lose that income. Quantifying the problem helps you figure out how much it is worth to you to solve it.

Dan Parker knows what his problem is: Should he start a web site design company? He took many computer courses throughout high school, and he is now attending college. He has worked in the food industry throughout high school and college to earn money to help pay for his college expenses. Dan enjoys working at restaurants and has gained valuable customer service and management experience. In addition, he also volunteers his web design skills on projects for his university and local community programs. He will be graduating in the next few months with a

degree in Computer Science. Dan is considering starting his own web site design business, but he is not sure whether that is the right choice for him.

Step 2 Gather Information

Once the problem has been defined, you need to gather information that could help solve it. Relevant information may be obtained from many sources, including company records, industry data, and trade magazines. It is also a good idea to interview other people in the industry to find out what their experiences have been and to learn how they have solved similar problems.

In Dan's case, it would be helpful for him to take a closer look at himself. He should do a self-assessment to determine his strengths and weaknesses. He also needs to consider his skills, experience, and interests. Does he have the characteristics of a successful entrepreneur? He also needs to examine the advantages and disadvantages of running a web site design company. He should talk to other professionals in the business and read trade magazines to gather information about running a web site design business. Dan needs to thoroughly explore every aspect of starting and running a web site design company.

Step 3 Identify Various Solutions

Most problems can be solved in various ways. Identify all possibilities before you settle on a particular solution. Dan comes up with several possible solutions to his problem.

1. Work as an employee in a position that utilizes his customer service skills and management experience.
2. Work as a web site designer for another company to gain more experience and then start his own business in three to five years.

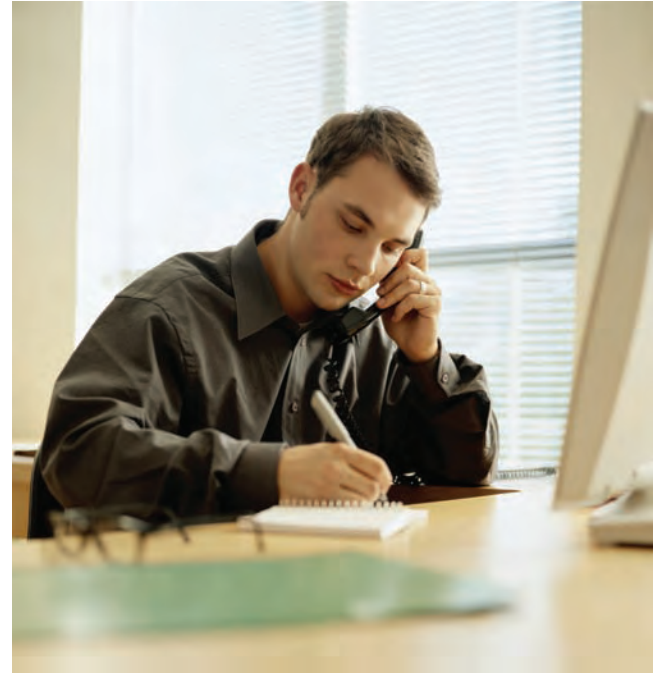


3. Pursue his interests in the food industry and open his own restaurant.
4. Start his own web site design company upon graduation.

Step 4 Evaluate Alternatives and Select the Best Option

The decision maker next needs to evaluate the alternatives to determine the best solution. In some cases, it may be possible to quantify the costs and benefits of each alternative. In other cases, quantifying each alternative may not be possible, and the decision maker may simply have to rank each alternative.

Dan ranks option 1 the lowest because of his strong desire to be his own boss. All of the information that Dan gathered indicates that he has a strong chance of succeeding as an entrepreneur. He ranks option 3 next to lowest. Dan has considerable experience in the food industry and enjoys that type of work, but he decides he would rather pursue his interests in web site design. He ranks option 2 second because he is already confident in his level of computer knowledge and experience. After evaluating all of his alternatives, Dan decides option 4 is the best solution.



© Getty Images/PhotoDisc

Why is it important to evaluate the decisions you make?

Step 5 Take Action

Once you have selected the best solution to the problem, you need to take action to implement it. Dan begins putting together a business plan and spreading the word about his new venture.

Step 6 Evaluate the Action

The problem-solving process is not complete until you evaluate your action since even a well-thought-out solution may not work. After being in business for six months, Dan evaluates whether he is achieving his financial and nonfinancial goals. It seems that Dan made the right decision because his business is profitable and he is enjoying his work. He has been able to fulfill his dream of working for himself while providing a valuable service to others. Dan will continue to use the problem-solving model to make the most effective decisions for his new business.

Checkpoint

What are the six steps in the problem-solving process?



Problem-Solving Skills

The more often you use the problem-solving model, the better skilled at decision making you will become. It will become a valuable tool to you throughout your career. There are a few other things you can do to improve your problem-solving skills.

Communicating

Good communication is important in the problem-solving process. When trying to resolve problems and make decisions, you most likely will have to interact with others. You may have to ask questions,

request information, and express your ideas and opinions. On such occasions, it is important that you communicate clearly and confidently. You must also be a good listener. You must carefully listen to information, opinions, and suggestions from others. Listening to others' input can help you make informative decisions.

Kris is the owner of a small boutique and is looking for ways to increase sales. She decides to conduct a meeting with her employees to communicate her sales objectives. During the meeting, she listens to her employees' thoughts and ideas for boosting sales. Through this communication process, Kris is able to gather lots of good information to help her solve her problem.



© Digital Vision

How can communicating with others help you succeed in business?

Brainstorming

Brainstorming is a creative problem-solving technique that involves generating a large number of fresh ideas. Brainstorming is often done in a group setting, but it is a very useful activity for an individual as well. Think about the problem you are trying to solve. Brainstorm by writing down as many possible solutions to the problem as you can think of. Do not be afraid to write down any idea you have. The point of brainstorming is not to judge your ideas as good or bad but to come up with as many ideas as possible. Once you have made a list of ideas, you can use the problem-solving model to determine the best alternatives.

Learning from Mistakes

If you want to become an entrepreneur, you cannot be afraid to make mistakes. Mistakes are likely to happen, but a negative can be turned into a positive. You should view your mistakes as a learning experience. Mistakes can help you learn what to do or what not to do, which proves to be valuable in the problem-solving process.

When you read about some of the nation's most famous entrepreneurs, you will find that many of them failed before they came up with a winning idea. Colonel Sanders of KFC fame is a good example. He held many jobs and owned a motel chain, service stations, and other restaurants that were unsuccessful. While running his restaurant, he developed his secret recipe chicken. In 1952, at the age of 62, he began traveling by car across the country selling his chicken. By 1964, there were 600 KFC restaurants in the United States and Canada, and Colonel Sanders sold KFC for \$2 million.

Checkpoint

How can you improve your problem-solving skills?

1.4 Assessment

THINK ABOUT IT

1. Must the six steps in the problem-solving model be performed in the order described? Why or why not?
2. How do you think strong communication skills can improve the problem-solving process? Provide specific examples of how a business owner might use communication skills to resolve a problem.

MAKE ACADEMIC CONNECTIONS

3. **MATH** In the Identify Various Solutions stage of the problem-solving model, you list a variety of possible solutions to a problem. For the four options Dan Parker came up with on pages 22–23, assign a percentage weight to each based on Dan's reasoning. Give the decimal equivalent for each percentage. What must the decimal value of the four options total?
4. **PROBLEM SOLVING** You own a successful shop that buys, sells, and services bicycles. In January, the owner of the building you now lease tells you that she has found a buyer for the property and plans to sell it in six months. Using the six-step problem-solving model, develop a plan for how to proceed.



TEAMWORK

Working as a team, identify some benefits to using a formal problem-solving method that are not given in the text. Provide some examples of how entrepreneurs might use the problem-solving model in their business.



Sharpen Your Entrepreneurial Skills



Effective Business Letters

As an entrepreneur, you might write letters to communicate your business ideas, solicit business, respond to customer questions, negotiate purchases, or deal with suppliers. To do so effectively, you need to develop your business writing skills. Writing a business letter is different from writing a letter to a friend. A certain level of formality is necessary, and certain standards must be followed. That doesn't mean business writing should be difficult to understand. Good business writing communicates ideas clearly. It also gets results by being positive and persuasive and by convincing readers that they should accept what the writer is communicating.

Certain basic rules should be followed in writing business letters as outlined below and as shown in the letter on the next page.

1. **Key all formal correspondence.** Send handwritten letters only when they are intended as personal letters.
2. **Spell all names correctly and have the correct address.** No matter how well written your letter is, its effect will be dramatically reduced if you misspell the name of the person to whom you are writing or refer to his or her company by the wrong name. Addressing a letter incorrectly may cause it to arrive late or to be returned.
3. **Always date your business correspondence.** It may be necessary to refer to this date at a later time.
4. **Use names and titles appropriately.** Use the person's first name if you know him or her well. If you do not know the person or the letter is very formal, use the person's last name, along with the appropriate title (Dr., Mr., Mrs., Ms., or Miss).
5. **Be direct and positive.** Always maintain a positive tone and portray your message in an optimistic light, even if your letter contains bad news.
6. **Be persuasive and specific.** Make sure the action or result you want from the reader is clear. Use nonthreatening language that will persuade the reader that this action or result is the most desirable.
7. **Avoid using fancy language.** Use straightforward language that says exactly what you mean.
8. **Be polite.** Deal with complaints in a businesslike fashion. Don't whine or express outrage, and never become abusive or insulting. Be especially polite in writing rejection or bad news letters.
9. **Use an appropriate closing.** Make sure your closing corresponds to the content of the letter you have written. If you have written

a letter to a supplier complaining about poor service, do not use “With warmest regards.” Common closings are “Sincerely” and “Sincerely yours.”

- 10. Proofread for spelling and grammatical errors.** The most persuasive and positive letter can be ruined by a single mistake.

Creative Web Designs

10 E. 34th Street • Baltimore, MD 21218
(410) 555-4321 CWD@internet.com

April 11, 20—

Ms. Chelsey Wright
Advantage Marketers
692 Kemper Road
Baltimore, MD 21209

Dear Ms. Wright

Are you looking for new ways to energize your web site? If so, I would like to introduce myself and talk with you about my company, Creative Web Designs.

As a recent graduate of Piedmont State University with an Associate degree in Computer Science, I am ready to put my skills to work for you. After providing web development services for the local university and for other local community programs for the past several years, I have decided to offer my services to other local businesses such as yours. Services provided include the following:

Creation of visibly appealing and compelling web pages

Revitalization of existing web sites

Hyperlink development

Technical support

Please call for a free consultation to discuss how you can have a web site that works effectively for your company. Samples of my web site creations are available for you to review. References can be provided upon request. I look forward to hearing from you.

Sincerely

Dan Parker

Dan Parker
Owner

TRY IT OUT

You own a shop that sells comic books. Write a business letter to your main supplier, a comic book wholesaler. Tell the supplier that you have not received the shipment you ordered of the most recent edition of a popular comic. Be sure to follow the basic rules for writing business letters. Make up names for your business and your supplier’s business.



© Stockbyte

Chapter 1 | Assessment

SUMMARY

1.1 All About Entrepreneurship

1. Entrepreneurship is the process of running a business of one's own. The person who owns, operates, and takes the risks of a business venture is called an entrepreneur.
2. More than 99.9 percent of the 25.8 million U.S. businesses are considered small companies. Small businesses contribute more to the U.S. economy than all large corporations combined.
3. Factors that contribute to a new business's success or failure include having adequate capital, providing a product or service that meets customer needs, and the owner's education level and business experience.

1.2 Is Entrepreneurship Right for You?

4. Successful entrepreneurs tend to be independent, self-confident, goal-oriented, and creative.
5. Entrepreneurs must have good team-building skills and be able to work well with others.
6. To determine whether entrepreneurship is for you, you will need to assess your strengths, weaknesses, interests, and aptitudes.

1.3 Exploring Ideas and Opportunities

7. Ideas for new businesses can come from many different sources, including your hobbies and interests, your past experiences, and from a discovery or invention.
8. You may investigate business opportunities through the Internet and public library, the Small Business Administration, trade shows, and other entrepreneurs.
9. Entrepreneurs should set SMART goals, which are specific, measurable, attainable, realistic, and timely.

1.4 Problem Solving for Entrepreneurs

10. A problem-solving model consists of six steps: define the problem, gather information, identify various solutions, evaluate alternatives and select the best option, take action, and evaluate the action.
11. There are several ways to improve problem-solving skills, including communicating, brainstorming, and learning from mistakes.

What do you know now?

Read Ideas in Action on page 3 again. Then answer the questions a second time. How have your responses changed?

VOCABULARY BUILDER

Match each statement with the term that best defines it. Some terms may not be used.

1. People who work for someone else
2. An evaluation of your strengths and weaknesses
3. A creative problem-solving technique that involves generating a large number of fresh ideas
4. Special meetings at which companies of the same or related industry display their products
5. People who own, operate, and take the risk of a business venture
6. Thoughts or concepts that come from creative thinking
7. The ability to learn a particular kind of job
8. The process of running a business of one's own

- a. aptitude
- b. brainstorming
- c. employees
- d. entrepreneurs
- e. entrepreneurship
- f. ideas
- g. opportunities
- h. self-assessment
- i. trade shows

REVIEW YOUR KNOWLEDGE

9. Barbara Wall had a great recipe for sweet bell pepper sauce. Her friend Lynne Wilson convinced her that they should go into business together and sell the sauce. They now ship J.T.'s Red Sauce to stores in 35 states. Wall and Wilson are examples of

a. intrapreneurs	c. employees
b. entrepreneurs	d. managers
10. Which of the following is *not* an example of an entrepreneur?

a. Diane Molberg started By Request, a successful home bakery business.
b. Donna Cook started a cleaning service 10 years ago.
c. Gwen Morgan manages The Secret Garden, a business owned by her sister.
d. Elmer Olsen created Bayfield Apple Jam and distributes the jam nationally.
11. Team members who have the right set of skills needed to get the job done are demonstrating —?—.
12. Jackson Hewitt Tax Service is an example of which type of business?

a. manufacturing business	c. retailing business
b. wholesaling business	d. service business
13. The plant where Goodyear tires are made is an example of which type of business?

a. manufacturing business	c. retailing business
b. wholesaling business	d. service business
14. According to the Small Business Administration's Office of Advocacy, how many new businesses survive for at least two years?

a. 67 percent	c. 25 percent
b. 44 percent	d. 10 percent

15. Which of the following is *not* an advantage of entrepreneurship?
 - a. Entrepreneurs are their own bosses.
 - b. Entrepreneurs can be creative.
 - c. Entrepreneurs take all the risks involved with starting a business.
 - d. Entrepreneurs can make large sums of money.
16. Which step of the problem-solving process involves performing research and interviewing customers, suppliers, and employees?
 - a. Define the problem.
 - b. Gather information.
 - c. Identify various solutions.
 - d. Evaluate alternatives.

APPLY WHAT YOU LEARNED

17. The six categories of privately owned businesses include manufacturing, wholesaling, retailing, service, agricultural, and mining and extracting. In small groups, compile a list of specific industries and companies that belong to each category of business. Share your results with the class.
18. Is your personality suited for becoming an entrepreneur? Using the Activity CD, open the activity “Entrepreneurship Aptitude Test.” Print a copy and complete the activity. What does the test indicate?



MAKE ACADEMIC CONNECTIONS

19. **MATH** Ellen Greenberg loves to make and fly kites. Ellen is planning to open a shop that sells custom-made kites. She asks for your advice to help her set financial goals. Ellen estimates that after expenses, she can make a \$15 profit on each kite she sells. If her annual income goal is \$15,450, how many kites will she have to sell? Assuming she can make only three kites per day and will work five days a week year round, is this goal realistic?
20. **HISTORY** Find information on the life and career of a famous historical entrepreneur. Find out information such as birthplace, type of business started, and what effect the person had on the economy and history. Is the business still operating? Write a short report about your findings.
21. **COMMUNICATION** For the above History question, find a creative way to present your findings to the class. Use visual aids, skits, costumes, games, and so on.

WHAT WOULD YOU DO?

Nancy and Gayle had been best friends since elementary school. During their senior year, Nancy told Gayle about an idea she had for a business in the local community. She had done some research and thought that her idea had a good chance of turning into a profitable business. After high school graduation, Nancy went off to college and Gayle stayed home and went to the local community college. Since Nancy had not acted on her business idea before leaving for college, Gayle decided that she would try to open a business using Nancy's idea. What do you think about Gayle's actions? Is she doing the right thing?



BUILD YOUR Business Plan *Project*

This activity will help you identify a business opportunity that may be right for you. You will use this business idea throughout the book.

1. Divide a sheet of paper into two columns. In the first column list all your interests. In the second column, list business opportunities that relate to each interest.
2. Make a list of your strengths and weaknesses. Compare this list with your list of business opportunities. For which business opportunities would your strengths most apply? For which business opportunities would your weaknesses hurt the most? Based on your strengths and weaknesses, cross out those business opportunities that no longer seem suitable for you.
3. Assess your aptitude, using the checklist in Lesson 1.2. Put a checkmark next to the business opportunities that relate to your aptitudes.
4. For the business opportunities remaining on your list, assess the advantages and disadvantages of each. Cross out any whose disadvantages outweigh its advantages.
5. Using the library or Internet, find and list sources of information that relate to the business opportunities that remain on your list. Locate at least one of these sources for each business opportunity and write a sentence stating the type of information contained in it. On your list, cross out business opportunities for which you could not find any information.
6. Choose one of the business opportunities remaining on your list. Based on this business opportunity, answer the six questions listed in the Compare Different Opportunities section in Lesson 1.3.
7. Set personal financial goals for a five-year period based on the business opportunity you chose. Demonstrate that your goals are SMART (Specific, Measurable, Attainable, Realistic, and Timely). Assume you will need to borrow money to get started. How much profit do you hope to make in one year? Three years? Five years? Next, set nonfinancial goals you hope to achieve with this business. Be sure to include specific activities for each goal.
8. Write a letter to potential customers about the goods or services your business will provide. On paper, plan a telephone conversation you will use as a follow-up to the letter. Work with a classmate and do a mock phone conversation based on your plan.
9. Plan ahead to prevent any problems that may arise in your business. Think of a problem that could occur and use the six-step problem-solving model to deal with it now. Brainstorm solutions on your own or with family members or friends.

Planning a Career in Human Services



"A new health club opened near my Grandma's house, and she absolutely loves going there. The club is open 24/7. As Grandma was a bit intimidated by the high-tech exercise equipment at the club, she's hired a personal trainer to help her learn how to use the equipment and to hold her accountable for her efforts. She says she feels much more energetic and relaxed than she used to. She's even considering joining the volleyball team that's been established for seniors."

In a high-tech, convenience-oriented society that often results in inactive lifestyles, how do individuals maintain physical fitness? When the weather prohibits outdoor activities, where can people go to exercise?

Fitness facilities provide the location, equipment, and instruction necessary for club members to exercise. Personal trainers help individual clients customize a workout plan that will help them achieve their personal fitness goals.

EMPLOYMENT OUTLOOK

- Faster than average growth is anticipated.
- Aging baby boomers, who hope to maintain fitness in later life, are fueling the demand for fitness workers.
- Parents' desire to keep children fit as well as employers who encourage employees to stay in shape will contribute to the ongoing need for fitness workers.

JOB TITLES

- Corporate Personal Trainer
- Fitness Advisor
- Certified Personal Trainer
- Fitness Consultant
- Personal Fitness Coach

NEEDED SKILLS

- A high school diploma and CPR certification are usually needed.
- Fitness certification from a reputable certification organization is required.
- Continuing education is often mandatory.
- Being physically fit and extroverted and having strong interpersonal skills is necessary.

What's it like to work in Human Services Nhu, a certified personal trainer, spent the weekend at a training seminar. The session was part of her ongoing training to stay current on developments in the personal training field.

This morning Nhu taught a group exercise class at a large fitness center. She enjoyed leading a large group of people and helping them improve their fitness level. The class also gave her the opportunity to meet a large number of health club members. Some of the class attendees signed up for her personal training services at the club.

Upon signing up for personal training, club members can work with Nhu on their individual fitness goals for an hourly fee. If they elect to buy a ten session pass, then the hourly fee is reduced.

Over the years, Nhu has also established a private personal training service. When she attends a client's home for a training session, she charges a higher hourly rate for the training. Many clients with busy schedules are more than happy to pay the higher rate to save the time of going to a gym.

What about you? Would you find it gratifying to help individuals improve their physical fitness levels?



PRESENTATION MANAGEMENT TEAM



Participants in this event will use current desktop technologies and software to prepare and deliver an effective multimedia presentation. A team will consist of two to four members. The team shall design a computer-generated multimedia presentation on the assigned topic. A new topic is selected by BPA every year. A word processed copy, including cited works, must be submitted at the time of the presentation. The team is to make effective use of current multimedia technology in the presentation (examples: sound, movement, digital video, and so forth). Space, color, and text should also be used effectively in the presentation.

TOPIC: Business Professionals of America is a forward-thinking organization. Your team has been asked to research three growing entrepreneurship opportunities for the next decade. You will develop a presentation on these trends for the BPA Board of Trustees, including new competitions to measure skills in these areas.

Participating teams will have from seven to ten minutes for oral presentations. Judges have an additional five minutes to ask questions about the presentation.

PERFORMANCE INDICATORS EVALUATED

- Evaluate and delegate responsibilities needed to perform required tasks.
- Demonstrate effective teamwork skills needed to function in a business setting.
- Demonstrate knowledge of multimedia software and components.
- Demonstrate effective oral communication skills.
- Apply technical skills to create a multimedia presentation which enhances the oral presentation.

Go to the BPA web site for more detailed information.

Think Critically

1. Why must entrepreneurs look at future trends when making business decisions?
2. Why should entrepreneurs look beyond current technology trends when making business decisions?
3. Why should statistics be used for this presentation?
4. How are entrepreneurs affected by a global economy?

www.bpa.org

Chapter 2

© Getty Images/PhotoDisc



Entrepreneurs in a Market Economy

2.1 Entrepreneurs Satisfy Needs and Wants

2.2 How Economic Decisions Are Made

2.3 What Affects Price?

school.cengage.com/entrepreneur/ideas

IDEAS IN ACTION

Web Site Design

Have you ever wondered why certain web sites come up when you use a search engine such as Google or Yahoo? The results you get may be due to the work of Exclusive Concepts, Inc.

Scott Smigler, Exclusive Concepts founder and president, balanced dual roles as a student and an entrepreneur through high school and college. His company provides professional web design and online marketing solutions by helping businesses design web sites that stand out when someone uses a search engine. Scott ran the company by himself in the beginning. Eventually, Scott moved from his home to his college dorm room to offices in Waltham, Massachusetts, and hired a staff of 15. The company's estimated sales for a recent year were \$1,200,000. Today, Scott Smigler continues to serve as CEO of Exclusive Concepts, and the company has grown five-fold.

Scott's ability to develop keyword strategies, write attention-getting keyword ad copy, create and optimize bidding strategies, and analyze results for continuous improvement helped him become a leader in the field. In addition to running the company, he maintained a 3.7 GPA as a finance major at Bentley College in Waltham, Massachusetts. He and Eric Golden, also a Bentley student, started the Bentley Entrepreneur Society to help other students with an interest in entrepreneurship.

Some important lessons Scott has learned include these:

- **Perseverance** Implementing dreams is not easy. You must be organized and focused.
- **Mentorship** Have a network of mentors to help you with problems.
- **Communication** You need excellent communication skills, and written agreements between your company and clients are essential.
- **Capitalization** Be prepared for everything to be more expensive than you think, and plan for unanticipated expenses.
- **Marketing** Everyone is a potential customer or client. Work to acquire new relationships while continuing to build existing ones.

Scott says that starting and running a business require focus, dedication, and time, but it is important to remember that there is life outside the business.

What do you know?

1. What type of interests do you think Scott had that helped him find success in this business?
2. Which of the lessons that Scott has learned do you think is most important?
3. Why do you think it is important to find a balance between work and play?



Scott Smigler, Exclusive Concepts founder and president

© www.ExclusiveConcepts.com
Photographer: David Fox

2.1

Entrepreneurs Satisfy Needs and Wants

Goals

- Distinguish between needs and wants.
- Describe the types of economic resources.
- Describe the role of entrepreneurs in the U.S. economy.

Terms

- needs
- wants
- economic resources

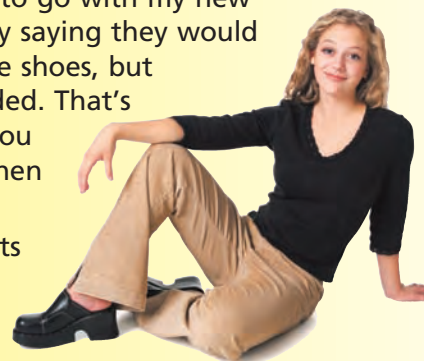
Focus on Economics

Do you *want* it or *need* it?

"Dad, I really need a new pair of shoes to wear to the Winter Dance," said Stephanie. "Do you *need* a new pair of shoes, or do you *want* a new pair of shoes?" her father responded. "Want or need—what's the difference?" Stephanie replied. Stephanie's father paused as he thought about the valuable lesson he could teach his daughter and then said, "That's a good question, Stephanie. Let's look at it this way. Do you really need the shoes in order to survive, or will having the new shoes make you feel better?"

Stephanie thought about what her father asked and said, "Well, Dad, it won't keep me from going to the dance if I don't have the new shoes, but I'd sure like to have new shoes to go with my new dress. So, I guess I'd have to answer you by saying they would make me feel better." "Then you *want* the shoes, but you don't *need* them!" her father responded. That's what economics is all about!" "Oh, Dad, you always try to teach me something even when I just want a new pair of shoes!"

Work as a Team Discuss needs and wants that you have. Do you sometimes have a difficult time telling the difference between a need and a want? Do you think peer pressure makes it more difficult to distinguish between a need and a want?



© Getty Images/PhotoDisc

It is often difficult to distinguish between a want and need.

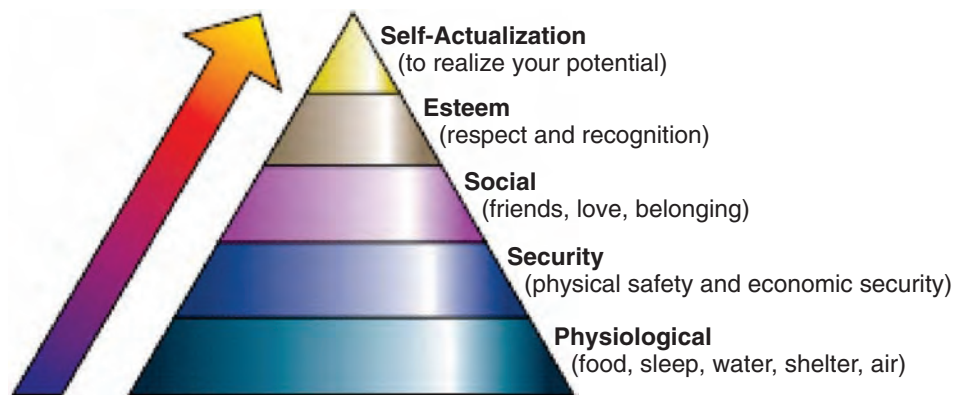
Is It a Need or a Want?

Think about your favorite piece of clothing. It may be a blouse, a favorite pair of jeans, or maybe the latest in designer shoes. First, you thought about what you wanted in clothing, and then you went out and found it. Maybe you looked at several articles of clothing and compared prices before you decided to spend your money. If someone else gave you clothing as a gift, then that person had to think about what you might like and then make a choice. Economics is all about making choices and satisfying the wants and needs of consumers.

Do you know the difference in your needs and wants? Your **needs** are things that you must have in order to survive. Needs include food, basic clothing, and a place to live. Your **wants** are those things that you think you must have in order to be satisfied. Wants add comfort and pleasure to your life. Wants would include things like CDs, computers, jewelry, and designer clothes. The role of business is to produce and distribute goods and services that people need and want.

Needs

People have many needs. Some are basic needs, while others are higher-level needs. Abraham Maslow was a psychologist who developed a theory on the *hierarchy of needs*. It identifies five areas of needs—physiological, security, social, esteem, and self-actualization needs. The theory suggests that people’s basic physiological needs, such as food, clothing, and shelter, must be satisfied first before they can focus on higher-level needs. Once basic needs are met, they will try to satisfy their security needs. When this need is filled, individuals turn their attention to social needs, such as friendship. Esteem needs can be satisfied by gaining the respect and recognition of others. Self-actualization needs usually involve something that provides a sense of accomplishment, such as earning a college degree.



Maslow's Hierarchy of Needs Pyramid

Beyond basic needs, not all people have the same needs. Needs depend on a person's situation. For example, you may live in a nice house in a gated community, so your security needs are met. Someone who lives in a high-crime area still may be trying to meet his or her security needs.

Wants

Individuals have two different types of wants—economic wants and non-economic wants. Economic wants involve a desire for material goods and services. They are the basis of an economy. People want material goods, such as clothing, housing, and cars. They also want services, such as hair styling and medical care. No economy has the resources necessary to satisfy all of the wants of all people for all material goods and services. The goods and services that people want must be produced. Clothes must be made, houses built, and cars manufactured. Personal services must be supplied.

★ Develop Your Reading Skills

As you read this chapter, develop an outline of the main topics. Write a short summary for each topic after you read it.



NETBookmark

Over the past several years, gasoline prices in the United States have been very unstable, changing drastically from week to week or even from day to day. Web sites such as GasBuddy.com help consumers find the lowest gas prices in their communities. Access school.cengage.com/entrepreneur/ideas and click on the link for Chapter 2. Use the chart of average gasoline prices to determine whether U.S. gas prices have increased or decreased in the past week. How about the past month or year? Click some of the Recent News links. What accounts for recent changes in gasoline prices?

school.cengage.com/entrepreneur/ideas

People also have noneconomic wants, or the desire for nonmaterial things. These wants would include such things as sunshine, fresh air, exercise, friendship, and happiness.

Needs and Wants Are Unlimited

Your needs and wants never end. You are limited only by what your mind can think of and what businesses make available for sale. If you are going camping, you might need to buy a tent for shelter. One purchase often leads to another. After buying a tent, you might also want to buy other camping supplies. Then you might want a bigger backpack to carry your new supplies.

Checkpoint

What is the difference between needs and wants?

Economic Resources

Economic resources are the means through which goods and services are produced. *Goods* are products you can see and touch. *Services* are activities that are consumed as they are produced. Entrepreneurs use economic resources to create the goods and services consumers use. Consumers satisfy needs and wants by purchasing and consuming goods and services. Goods are products you can purchase. A pair of shoes, a jacket, food, and cars are all examples of goods. Services must be provided to



What kind of resources are used for farming?

you at the time you need them—they cannot be stored. A haircut, a pedicure, lawn mowing, and car detailing are all examples of services.

Factors of Production

In order to create useful goods and services, an entrepreneur may use three types of economic resources. These resources are called the *factors of production* and include natural resources, human resources, and capital resources.

NATURAL RESOURCES Raw materials supplied by nature are *natural resources*. The earth contains oil, minerals, and the nutrients needed to grow crops and timber. Rivers, lakes, and oceans are the sources of both food and water. All products you use begin with one or more natural resources. The supply of many natural resources is limited. Increased use of natural resources and damage to the environment threatens the continued availability of natural resources in many regions of the world. Conservation practices and the production of more efficient products help to preserve and renew resources. Compact fluorescent light bulbs (CFLs) cost more than old-style incandescent bulbs, but they last longer, use far less electricity, save consumers' money in the long run, and reduce greenhouse gases. When consumers switch to CFLs, they help preserve energy resources and the environment for future generations. One CFL keeps a half-ton of greenhouse gases (CO₂) out of the atmosphere.



How do compact fluorescent light bulbs save energy?

© The Image Bank/Getty Images

HUMAN RESOURCES The people who create goods and services are called *human resources*. They may work in agriculture, manufacturing, distribution, or retail businesses. As an entrepreneur, you would also be a human resource. Entrepreneurs have creative ideas and use these ideas to create new goods and services, which in turn give consumers more choices.

CAPITAL RESOURCES The assets invested in the production of goods and services are called *capital resources*. Capital resources include buildings, equipment, and supplies. They also include the money needed to build a factory, buy a delivery truck, and pay the employees needed to manufacture and distribute goods and services.

Limited Resources

All economic resources have a limited supply. Most resources can be used to produce several different products and services. If resources are used to produce one type of product, they may not be available for the production of another product. Individuals, businesses, and countries compete for access to and ownership of economic resources.



Those resources that are in very high demand or that have a limited supply will command high prices. Because there is a limited amount of natural resources, there will also be a limit to the amount of goods and services that can be produced. Control of oil fields in the Middle East has been an ongoing issue for many years. The United States has a large demand for oil but a limited supply of oil, so it is important to the United States to have access to oil from the Middle East. This high demand contributes to high gasoline prices.

Checkpoint

List the three types of economic resources and give an example of each.

Role of Entrepreneurs in the U.S. Economy

Entrepreneurs play an important role in the U.S. economy. Because all businesses that exist in the United States today began as an entrepreneurial idea, you could say that entrepreneurs are the backbone of the U.S. economy. The development and growth of small businesses help to ensure a strong economic future.

Supply and Demand

As business owners, entrepreneurs play an important role in supplying goods and services to meet the demands of consumers. They look for unmet needs or better ways to satisfy consumer needs and wants. They use resources and their knowledge of markets and business to efficiently produce goods and services that meet consumer needs and wants.

Capital Investment and Job Creation

In order to start businesses, entrepreneurs need money to finance their businesses. Sometimes they will use their own money. Other times, they will look to investors and lenders to supply them with the money they need to get started. They may use the money to lease a building, buy equipment, or hire employees. By doing so, entrepreneurs are investing in



How do small businesses contribute to the local economy?

© Blend Images

their communities by contributing to the local economy and providing jobs.

Change Agents

Many entrepreneurs create products that change the way people live and conduct business. When you learn about American history, you see that many entrepreneurs have shaped the U.S. economy. As entrepreneurs create more goods and services, consumers have more wants and needs. Entrepreneurs will always play an important role in the U.S. economy.

Checkpoint

What are some things entrepreneurs contribute to the U.S. economy?

2.1 Assessment

THINK ABOUT IT

1. What role do needs and wants play in determining what is produced in an economy?
2. Think of something that you would describe as a “need” but your parents would describe as a “want.” Provide reasons to support both sides of the argument.
3. How does the availability of economic resources affect decisions that entrepreneurs make?
4. Which of the contributions to the U.S. economy that entrepreneurs make do you think is most important? Why?

MAKE ACADEMIC CONNECTIONS

5. **SOCIAL STUDIES** Think of a business in your area. Make a list of the resources that the business uses for each factor of production.
6. **COMMUNICATION** Find information on the number of small businesses in the United States, the number of individuals employed by small businesses, the number of new businesses that open each year, and the number of business failures each year. Prepare a poster with this information and explain your findings to your classmates.



TEAMWORK

Working in a team, make a list of the natural resources in your area. Using the Internet, almanacs, and other information about your community, find out the impact these resources have on your local economy. Which businesses use these natural resources? What financial contributions to your local economy do these businesses make?



2.2

How Economic Decisions Are Made

Goals

- Compare different types of economic systems.
- Describe the characteristics of the U.S. economy.
- Explain how scarcity affects economic decisions.
- Explain how business functions are used to satisfy consumers.

Terms

- capitalism
- profit
- economic decision making
- scarcity
- opportunity cost

Focus on Economics

Choose between alternatives

"Stephanie, weren't you thinking about buying a new MP3 player last week?" her dad asked. "Yes, Dad, I was," Stephanie replied, "but if I buy the new shoes I want for the Winter Dance, I won't have enough money to buy the MP3 player now." "You've just learned a lesson about opportunity cost," her dad said. "What's that?" Stephanie asked. Her dad explained that when you choose one item over another, the opportunity cost is the value of the item you give up—in this case, the MP3 player. "I understand, Dad. But if you took this opportunity to buy the shoes for me, then I wouldn't have any opportunity cost, would I?"

Work as a Team Discuss choices that you have made recently. Did you realize that when you choose one item over another that there is an opportunity cost involved?



© Getty Images/PhotoDisc

You often have to choose one option over another.

Economic Systems

Different economic systems exist throughout the world. However, all economies must answer three basic questions.

1. What goods and services will be produced?
2. How will the goods and services be produced?
3. What needs and wants will be satisfied with the goods and services produced?

If all economies struggle with the same basic questions, what is it that makes economies different? The type of economic system that a country has will determine how these three economic questions are answered. Economies must choose a way to allocate, or distribute, the

goods and services that are available to the people who need or want them. These different allocation processes are what create different economies. Different economies have different ways of choosing which goods and services are produced, which needs are satisfied, and how many resources are used to satisfy those needs.

Command Economy

In a *command economy*, the government determines what, how, and for whom products and services are produced. Because the government is making the decisions, there is very little choice for consumers in what is available. The government may see no reason to have more than one type of the same item. This means individuals may not always be able to obtain exactly what they want. There will be shirts and pants, but there will not be many styles and colors from which to choose.

Market Economy

Market economies are about personal choice. In a *market economy*, individuals and businesses decide what, how, and for whom goods and services are produced. Entrepreneurship thrives in a market economy. Decisions about production and consumption are made by millions of people, each acting alone. Individual choice creates the market, so there are many items available that are very similar. If a good sells, it will remain on the market. If not, the good will not continue to be produced. There will be many styles of shirts and pants to appeal to every taste, but a manufacturer will not continue to produce a style that few or no people buy.

Individual choice also exists in how items are produced. A furniture maker will make choices regarding the style, fabric, and durability of products made. In addition, products and services are always available to everyone who has the means to pay for them.



© Getty Images/PhotoDisc

What effect does the economic system have on the product choices you have for clothing?

Traditional Economy

Before complex economic systems developed, simple economies operated according to tradition or custom. In a *traditional economy*, goods and services are produced the way they have always been produced. The traditional economy is used in countries that are less developed and are not yet participating in the global economy. Most of what is produced is consumed and what is left over is sold or traded with people who live in nearby communities. Traditional economies lack the formal structure found in more advanced economic systems and usually have limited capital resources available to improve their conditions.



Mixed Economy

When elements of the command and market economies are combined, it is called a *mixed economy*. A mixed economy often results when a country shifts away from a command economy toward a market economy but still has government involvement in the marketplace. Many countries are making this shift. During the last decade, several European nations that used a command economy have made progress toward creating a mixed economy. Several of these countries recently joined the European Union.

For over 70 years, the Soviet Union operated under a command economic system called *communism*. During this time, a series of government-led plans directed resources toward economic growth. The government control resulted in limited choices and a shortage in supply of many consumer goods. The Soviet Union disbanded and became 15 independent states in the early 1990s, resulting in a move toward market economies.

China operates under a different type of communist government that controls most of the resources and decisions. The economy of China is adopting elements of a market system for a growing number of economic decisions. China is fast becoming a world leader in goods and services produced. A competitive educational system in China produces many skilled workers who are opening businesses daily.

As many countries with traditional economies develop, they often adopt mixed economies. The government makes many of the decisions about how the country's resources will be used to develop schools, hospitals, roads, and utilities. As people become educated, they are able to obtain jobs and earn money. Then they have the resources to purchase more goods and services. Often businesses from other countries will begin to sell products and services in the developing country or open a business offering jobs to the citizens.

Famous Entrepreneur

Paul Revere

Paul Revere is best remembered as an American patriot who made a famous midnight ride, warning people that the British were coming. However, Paul Revere was also a successful entrepreneur. Trained as a silversmith, he used his engraving skills to create political cartoons to contribute to the movement for independence. He manufactured gunpowder, bullets, and cannons during the Revolutionary War. Afterwards, he developed new methods for his trade

and founded the Revere Copper Company in 1801. The original company evolved into Revere Copper and Brass, Inc., which today manufactures cookware that bears his name, a sure sign that his business lives on!

Think Critically

Paul Revere was able to use his silversmith skills when starting his business. How important do you think it is to have a skill that you can use when starting a business?



© Getty Images/PhotoDisc

Why do you think Paul Revere was a successful entrepreneur?

Checkpoint

How does the type of economy affect the way the basic economic questions are answered?

The U.S. Economic System

What type of economic system do you think the United States has? To answer this question, you must look at who makes most of the decisions about what is produced and consumed. Since individual businesses and consumers make most of these decisions, the U.S. system is best described as a market economy. **Capitalism**, which is the private ownership of resources by individuals rather than by the government, is another name for the economic system in the United States. Another term often associated with the U.S. economy is *free enterprise*, due to the freedom of businesses and individuals to make production and consumption decisions. This individual freedom is vital to the success of the U.S. economy.

The U.S. economic system is based on four basic principles: private property, freedom of choice, profit, and competition.

PRIVATE PROPERTY As a U.S. citizen, you can own, use, or dispose of things of value. You are free to own anything you want, and you can decide what to do with it as long as you operate within the law.

FREEDOM OF CHOICE You can make decisions independently and must accept the consequences of those decisions. Business owners are free to choose where to open a business, what to sell, and how to operate the company. Consumers are free to choose where to shop, what to buy, and how much they want to spend. Only when individual decisions will bring harm to others does the government regulate freedom of choice.

PROFIT The difference between the revenues taken in by a business and the costs of operating the business is called **profit**. The opportunity to earn a profit is at the heart of the free-enterprise system. One of the main reasons entrepreneurs invest resources and take risks is to make a profit. No business is guaranteed to make a profit, so entrepreneurs are challenged to work hard, invest wisely, and produce goods and services that consumers are willing to buy.

COMPETITION The rivalry among businesses to sell their goods and services is called *competition*. Consumers choose products and services based on the value they think they will receive. Competition forces businesses to improve products, keep costs low, provide good customer service, and search for new ideas so that consumers will choose their products or services.

Checkpoint

Describe the four basic principles of the U.S. economic system.



Economic Choices

Individuals and businesses are faced with economic choices every day. Decisions about needs and wants must be made. **Economic decision making** is the process of choosing which needs and wants, among several, you will satisfy using the resources you have. Two factors commonly enter into economic decision making—scarcity and opportunity cost.

Scarcity

In every economy, there are limited resources to produce goods and services. However, individuals have unlimited needs and wants. This produces the basic economic problem of scarcity. **Scarcity** occurs when people's needs and wants are unlimited and the resources to produce the goods and services to meet those needs and wants are limited. For example, land is a scarce resource. Land is used for many purposes, such as for growing crops or as a site for a business or house. The same parcel of land cannot be used to meet all of these needs. A decision on how to use it must be made. Land derives its value from its scarcity.

Decisions based on scarcity affect everyone. Individuals and families have many wants and needs. They must decide how to spread their income among all these wants and needs. City, state, and national governments collect taxes from their citizens. They must decide how to use the tax collections to provide all the services that citizens expect. In both cases, someone must make difficult choices.

Scarcity forces you to make choices or decisions. Suppose you work a part-time job and earn \$150 a week. If you decide to purchase a \$75 concert ticket and you owe \$75 for your monthly car insurance payment, you will not have any money left over to go out for pizza with your friends. Because you have only \$150, you have limited resources. With limited resources, you cannot afford to buy everything you want. You may have to make a *tradeoff* by giving up something so that you can have something else.

Opportunity Cost

When trying to satisfy your wants and needs, you most likely will have many alternatives from which to choose. Economic decision making will force you to explore all of your alternatives. The problem-solving process can be used to help you select the best and most satisfying alternative from a set of choices. When examining all of your alternatives, you should consider the opportunity cost of each one. **Opportunity cost** is the value of the next-best alternative—the one you pass up. If your grandparents give you \$300 for graduation, you have to decide what to do with it. If you decide to save the money for college, the opportunity cost would be the new iPod that you really wanted and could have purchased with the money.

Diane Mayfield has \$2,500 in extra cash that she wants to invest in her cake decorating business. Diane could use the money for advertising or she could purchase new equipment. If she decides to use the money for advertising, she will not be able to purchase new equipment.

did you KNOW?

According to the World Water Council, by 2025, approximately 3.5 billion people will live in places where water is scarce or is becoming scarce.



The opportunity cost of advertising will be the value of the new equipment—the next best alternative. Like all entrepreneurs, Diane will have to choose between various investment options.

Checkpoint

What factors affect economic choices?

Functions of Business

In a market economy, an entrepreneur is free to produce and offer to consumers any legal product or service. Knowledge of business activities will help entrepreneurs satisfy customers and make a profit. These activities or *functions of business* include the following:

- production
- management
- marketing
- finance

Each of these functions is dependent on the others in order for the business to be effective. Products can be produced, but if management is not functioning properly, if adequate financial records are not maintained, or if marketing is not getting the word out to consumers, the products probably will not be sold at a profit.

PRODUCTION The primary reason a business exists in a market economy is to provide products or services to consumers and to earn a profit. The production function creates or obtains products or services for sale.

MARKETING All businesses in a market economy need to complete marketing activities in order to make their products and services available to consumers. These activities make up the *marketing mix*, which includes the following:

- product
- price
- distribution
- promotion

The goal is to attract as many customers as possible so that the product succeeds in the marketplace.

MANAGEMENT It is necessary for all businesses in a market economy to spend a great deal of time developing, implementing, and evaluating plans and activities. Setting goals, determining how goals can be met, and deciding how to respond to the actions of competitors is the role of management. Management also solves problems, manages the work of employees, and evaluates the activities of the business.

BE YOUR OWN BOSS

You are planning to open a sandwich shop. You begin to think about the four functions of business—production, marketing, management, and finance. Describe how each function will apply to your business. Explain how the functions will work together to ensure you run a successful sandwich shop. Be prepared to share your ideas with your classmates.

FINANCE One of the first responsibilities of finance is determining the amount of capital needed for the business and how the capital will be obtained. The finance function also involves planning and managing the financial records of the business.

Checkpoint

What are the functions of business?

2.2 Assessment

THINK ABOUT IT

1. Prepare a chart showing how the three basic economic questions are answered by a command, a market, and a traditional economy.
2. Explain the contributions of the four basic principles to the success of the U.S. economy.
3. Opportunity cost can affect you personally. Name an item you have wanted to purchase but have not bought because you wanted another item more.
4. Why is it important for all functions of business to work together?

MAKE ACADEMIC CONNECTIONS

5. **MATH** David Kalb started a pet-walking business in New York City. He charges \$20 to walk one dog twice a day. He walks six dogs five days a week for four customers. He walks three dogs seven days a week for three other customers. How much money does David get from his customers each week? If his expenses each week total \$350, how much profit is he making weekly?
6. **ECONOMICS** Research the economic system of another country. Explain the type of economic system the country has and the effect it has on the lives of the people in the country. Describe how the economic system would affect entrepreneurs in the country.
7. **PROBLEM SOLVING** You worked for your grandmother doing odd jobs around her house. She paid you \$75 for the work you did. You need \$25 to fill your car with gasoline for the upcoming week, \$10 for school lunch, \$40 for prom tickets, and \$30 for a deposit on your tuxedo/dress for the prom. How much money do you still need to cover all your expenses? Since your resources are limited, use the problem-solving process to decide how to spend the \$75. Explain your choices.



TEAMWORK

Working in a team, choose a business with which you are familiar. For the business you choose, make a list of the activities that would take place involving each of the four functions of business.

2.3 What Affects Price?

Goals

- Explain how supply and demand interact to determine price.
- Describe how costs of doing business affect the price of a good or service.
- Explain the effect of different market structures on price.

Terms

- supply
- demand
- equilibrium price and quantity
- fixed costs
- variable costs
- marginal benefit
- marginal cost

Focus on Economics

Does supply match demand?

"Well, Dad, I went to the mall today to buy my new shoes and nobody had the ones I wanted," Stephanie told her father. "Every store I went to said it had sold out of the shoes because they were on sale. The manufacturer is supposed to send another shipment of the shoes next week." "Oh," her father said, "so more people want the shoes because the price is lower. And the manufacturer is willing to make more shoes even at the lower price because it is still making a profit. This is the law of supply and demand at work." "Dad, there you go again—always trying to make a point!"

Work as a Team In the U.S. economy, you have many choices, but sometimes you might not be able to find exactly what you want. Think of products that you have wanted to buy but could not find. Why do you think you could not find them?



Manufacturers must try to keep up with product demand.

How Much Is Enough?

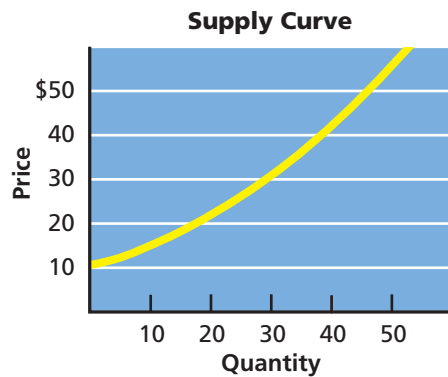
If a market economy is based on personal choice, why does there always seem to be just enough of everything? In a market economy, individual consumers make decisions about what to buy, and businesses make decisions about what to produce. Consumers are motivated to buy goods and services that they need or want. Business owners are driven by the desire to earn profits. These two groups, consumers and producers, together determine the quantities and prices of goods and services produced.

Supply and Demand

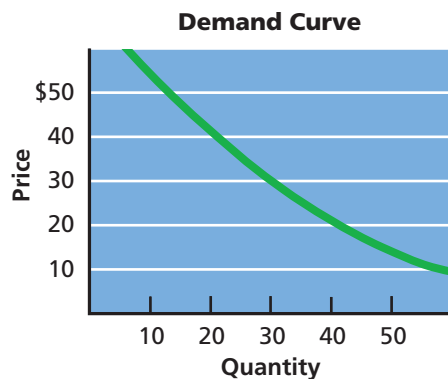
To understand how this works, you need to understand two important forces: supply and demand. **Supply** is how much of a good or service a producer is willing to produce at different prices. Imagine

that you supply car detailing services. Suppose that at a rate of \$40, you are willing to spend eight hours a week providing car detailing services. If your customers are willing to pay just \$20 for a car detail, you might decide not to bother detailing cars at all. If, however, the rate for car detailing rose to \$60, you would probably increase the number of cars you would detail. You might even try to get some friends to help you detail even more cars.

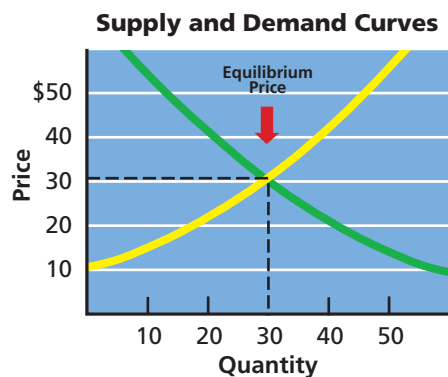
As the price of car detailing services rises, suppliers are willing to provide more services. The quantity of car detailing services supplied rises as the price for car detailing services increases, as shown on the supply curve graph.



Suppliers are willing to supply more of a product or service at a higher price.



Individuals are willing to consume more of a product or service at a lower price.



The point at which the supply and demand curves intersect indicates the equilibrium price and quantity. The equilibrium price is \$30 a unit, and 30 units will be produced.

Now consider the demand side of the market economy.

Demand is an individual's need or desire for a product or service at a given price. Suppose that you are interested in having your car detailed. At a rate of \$40, you figure it is worth having your car detailed once a month. If, however, the rate fell to just \$20, you might be willing to have your car detailed twice a month.

As the price of the service or product decreases, consumers are willing to purchase more of the product or service. Demand rises as the price falls, as shown on the demand curve graph.

When the demand of a product is affected by its price, this is referred to as *demand elasticity*. When a change in price creates a change in demand, you have *elastic demand*. When a change in price creates very little change in demand, you have *inelastic demand*. Demand is usually inelastic when

- There are no acceptable substitutes for a product that consumers need
- The change in price is small in relation to the income of the consumer, so consumers will continue to buy the product if they want it
- The product is a basic need for consumers, rather than just a want

When Supply and Demand Meet

How do the forces of supply and demand work together to determine price in a market economy? The point at which the supply and demand curves meet is what is known as the **equilibrium price and quantity**. This is the price at which supply equals demand. Above the equilibrium price, fewer people are interested in buying goods and services. At this point, suppliers will not be able to sell as much of their goods or services as they would like because they have priced them too high. Below the equilibrium price, the price is too low. Consumers would be very happy to purchase many of the goods or services at these prices, but suppliers would not be willing to produce enough to meet their demand. Only at the equilibrium price does the amount consumers want to buy exactly equal the amount producers want to supply.

Checkpoint

What effect do supply and demand have on the price of a good or service?

Costs of Doing Business

To determine how much profit they are earning, entrepreneurs need to know how much it costs to produce their goods or services. To do so, they must consider all the resources that go into producing the good or service to determine a price to charge.

The Jewel Box, a small company that produces handmade jewelry, requires office space, materials, labor, and equipment. All of these resources go into making a piece of jewelry, and all of them must be taken into account when figuring out the price. A company that prices its product based only on the cost of materials involved in producing it will lose money and go out of business very quickly.

Fixed and Variable Costs

Every business has fixed costs and variable costs. **Fixed costs** are costs that must be paid regardless of how much of a good or service is produced. Fixed costs are also called sunk costs. **Variable costs** are costs that go up and down depending on the quantity of the good or service produced.

To understand the difference between fixed and variable costs, consider The Bread and Bagel Shop, a small business owned by entrepreneur Michael Miller. Whether or not customers buy his baked goods, Michael pays the same monthly rent, the same insurance fees, and the same interest on the loans taken out to finance his business. These are Michael's fixed costs. He must pay them even if The Bread and Bagel Shop makes no sales. The store also has variable costs, including the expense of buying flour, sugar, and coffee. These expenses rise directly with the number of items sold. The more bagels, donuts, and cups of coffee the company sells, the more resources it must buy to make more goods. In contrast, when customers purchase fewer loaves of bread, Michael uses less flour and other ingredients.

Understanding the difference between fixed and variable costs is important. A business with many fixed costs is a higher risk than a business with mostly variable costs, because fixed costs will be incurred regardless of the level of sales. If sales turn out to be much lower than expected, the business will be stuck with many bills to pay and little revenue to cover them.



© Getty Images/PhotoDisc

If bread sales increase at a bakery, how might this affect its variable costs?

Marginal Benefit and Marginal Cost

Entrepreneurs make business decisions based on the concepts of marginal benefit and marginal cost. **Marginal benefit** measures the advantages of producing one additional unit of a good or service.

Marginal cost measures the disadvantages of producing one additional unit of a good or service.



Michael Miller of The Bread and Bagel Shop wants to increase his sales. Michael is considering keeping the store open two extra hours every day. He estimates that during the last two hours of every day, he will sell an additional 150 baked goods and 30 cups of coffee, bringing in additional daily revenues of \$100. This \$100 represents the marginal benefit of keeping the store open an extra two hours a day.

Should Michael stay open two extra hours each day? To figure out if staying open later makes economic sense, Michael needs to figure out the marginal cost of staying open later. He will need to purchase additional ingredients to produce another 150 baked goods and 30 cups of coffee. He will have to pay overtime wages to at least two employees. He will also use more electricity. Adding up these costs, Michael estimates that staying open two extra hours will cost him \$125 a day. Because the marginal cost of staying open (\$125) exceeds the marginal benefit (\$100), Michael decides not to change the store's hours.

Checkpoint

How do the costs of doing business affect prices?

Market Structure and Prices

Market structure is determined by the nature and degree of competition among businesses that operate in the same industry. The main criteria used to distinguish between different market structures are the number and size of sellers and buyers in the market, the type of goods and services being traded, and the barriers to entry into the market for sellers. There are four major market structures: perfect competition, monopolistic competition, oligopoly, and monopoly. Each market structure has an effect on the prices businesses can charge for their products or services.

Perfect Competition

A market with *perfect competition* consists of a very large number of businesses producing nearly identical products and has many buyers. Buyers are well-informed about the price, quality, and availability of products. Because consumers have so many choices of similar products, price is often the deciding factor, making it difficult for a single business to raise prices. This gives consumers more control of the market. Businesses can easily enter or leave this type of market. Examples of industries in perfect competition include gasoline suppliers and producers of agricultural products such as wheat and corn.



What kind of competition do you think a vacuum cleaner manufacturer faces?

Monopolistic Competition

A market with *monopolistic competition* has a large number of independent businesses that produce goods and services that are somewhat different. Each business has a very small portion of the market share. This is also called a competitive market. In a competitive market, many suppliers compete for business, and buyers shop around for the best deal they can find. In this kind of market, prices are said to be determined competitively. Products offered are not identical but very similar, so differentiating products becomes very important. Businesses can easily enter or leave a market that has monopolistic competition. Businesses in monopolistic competition include retail stores and restaurants.

Oligopoly

When a market is dominated by a small number of businesses that gain the majority of total sales revenue, it is called an *oligopoly*. Businesses in this market sell similar goods and services that are close substitutes, and they have influence over the price charged. With the dominance of a few businesses, it is not easy for new ones to enter the industry. Examples of oligopolies include the automobile and airline industries.

WHAT WENT WRONG ?

Avoid personal debt

Dave McClure, a Silicon Valley entrepreneur with no previous business experience, took on a great amount of debt when he founded a Web and database services company. He founded Aslan Computing in 1995. He used his own personal savings and took out a second mortgage on his home to get the money he needed to get his business off the ground. At first, it appeared that Dave's venture was successful. He made \$1.8 million in sales within two years. Upon closer examination of his financial records, however, things did not look as good. Although Dave's business generated a large amount of revenue, it did not generate much profit. Aslan Computing's costs exceeded its revenues, and it incurred a net loss of \$50,000 the second year. On the brink of collapse, no bank would lend Dave additional funds. His credit card debt peaked at \$120,000. Friends urged him to bail out before things got worse. He managed to sell the business for enough money to pay off his debts.

Think Critically

1. Do you think it is wise for a business owner to take on a large amount of personal debt when starting a business?
2. What other options does an entrepreneur have if no bank is willing to loan money to help finance the business?



© Digital Vision

When starting your business, be sure to avoid personal debt.

Monopoly

Where there is only one provider of a product or service, a monopoly exists. A company that has a *monopoly* is able to charge whatever price it wants, because consumers have nowhere else to go to find a better price. This is the opposite of a competitive market where consumers can simply switch to a lower-priced good or service offered by a competitor. The one provider can raise prices up to the point where consumers will choose to simply do without the product or service. Monopolies usually exist because of barriers that make it difficult for new businesses to enter the market. Examples of monopolies include local water and electric utility companies.

Checkpoint

How does the market structure affect the price of a good or service?

2.3 Assessment

THINK ABOUT IT

1. Have you ever wanted to buy something, but you couldn't find it? What role do you think supply and demand might have played?
2. Name three fixed costs in your life. How do you plan to pay them? Name three variable costs that you have. How can variable costs be like opportunity costs?
3. Think of an item you purchase often. If the price is similar at several stores, do you always buy at the same store? Why or why not?
4. Describe the important features of each of the market structures.

MAKE ACADEMIC CONNECTIONS

5. **COMMUNICATION** Find advertisements for two competing products. Analyze the ads to see how the products are differentiated. Make a poster of the two ads and label the items that are different.
6. **ECONOMICS** Create a table with two columns. In the first column, list the four market structures. In the second column, list five to ten goods or services that would be available in each of the different market structures.



TEAMWORK

Working in a team, brainstorm a list of businesses in your state and your local area. Discuss with your teammates the type of market structure in which you think each business operates. Give reasons for your choices. Share your list with your classmates.



Sharpen Your Entrepreneurial Skills

Effective Presentation Skills

Much of your communication as a business owner will be conducted verbally. You may have to make a presentation to sell your business idea to potential investors, or you may have to make a presentation before potential customers to convince them to purchase your product or service. How you present yourself will have a big impact on the people with whom you deal.

When preparing a presentation, you should be concise, but give adequate information to cover the topic being presented. An effective presentation has three parts.

1. **Introduction** You should begin your presentation with an attention-getting opener that introduces your topic. Asking a question or using a famous quote is a good way to get your audience focused on the topic.
2. **Body of Presentation** Try to limit your presentation to three main points. It is often helpful to provide a visual aid that lists your key points. Do not overwhelm your audience with too much detail. Use facts and other supporting information to reinforce your main points. Keep the presentation simple and avoid using complicated language.
3. **Conclusion** After presenting your main points, summarize what you have told your audience in a brief conclusion.

TRY IT OUT

To practice your presentation skills, research an entrepreneur who you believe has been a change agent. Prepare an effective presentation for the class explaining the impact this entrepreneur has had on other people's lives.



© Digital Vision

Chapter 2 | Assessment

SUMMARY

2.1 Entrepreneurs Satisfy Needs and Wants

1. Economics is all about making choices and satisfying the needs and wants of consumers. Your needs are things you must have to survive. Your wants are things you think you must have to be satisfied.
2. Three kinds of economic resources are used by entrepreneurs to produce goods and services—natural resources, human resources, and capital resources.
3. Entrepreneurs play an important role in the U.S. economy. They supply goods and services, provide capital investment and job creation, and serve as agents for change.

2.2 How Economic Decisions Are Made

4. There are four kinds of economic systems—command economy, market economy, mixed economy, and traditional economy.
5. The U.S. economic system is based on the principles of private property, freedom of choice, profit, and competition.
6. Economic choices are necessary because of our unlimited desires and the scarcity of resources available to satisfy them. Every economic decision involves an opportunity cost.
7. The functions of business are production, marketing, management, and finance. Each function is dependent on the others.

2.3 What Affects Price?

8. Supply is how much of a good or service a producer is willing to produce at different prices. Demand is an individual's need or desire for a product or service at a given price. The point at which supply equals demand is the equilibrium point.
9. Entrepreneurs must consider all the resources that go into producing a good or service to determine a price. Fixed costs remain the same regardless of how much of a good or service is produced, while variable costs go up and down depending on the level of production.
10. Market structure is determined by the nature and degree of competition among businesses that operate in the same industry. The four major market structures are perfect competition, monopolistic competition, oligopoly, and monopoly.

What do you know now?

Read Ideas in Action on page 35 again. Then answer the questions a second time. How have your responses changed?

VOCABULARY BUILDER

Match each statement with the term that best defines it. Some terms may not be used.

1. Those things that you think you must have in order to be satisfied
2. The means through which goods and services are produced
3. Occurs when people's needs and wants are unlimited and resources are limited
4. The process of choosing which wants you will satisfy using the resources you have
5. The value of the next-best alternative—the one you must pass up
6. Point at which supply and demand meet
7. Measures the advantages of producing one additional unit of a good or service
8. Private ownership of resources by individuals
9. An individual's need or desire for a product or service at a given price
10. Costs that go up and down depending on the quantity of the good or service produced

- a. capitalism
- b. demand
- c. economic decision making
- d. economic resources
- e. equilibrium price and quantity
- f. fixed costs
- g. marginal benefit
- h. marginal cost
- i. needs
- j. opportunity cost
- k. profit
- l. scarcity
- m. supply
- n. variable costs
- o. wants

REVIEW YOUR KNOWLEDGE

11. An example of a noneconomic want is
 - a. clothing
 - b. housing
 - c. friendship
 - d. cars
12. Which of the following is *not* an example of a service?
 - a. lawn care
 - b. car wash
 - c. television
 - d. cable TV installation
13. If a product has inelastic demand, a price increase will cause
 - a. consumers to buy more
 - b. competitors to enter the market
 - c. consumers to buy less
 - d. little or no change in the demand for the item
14. What determines the type of economic system a country has?
 - a. the political beliefs of the country's ruler
 - b. the way the basic economic questions are answered
 - c. the resources of the country
 - d. the demands of the people
15. What are the three basic economic questions countries must answer?
16. Which of the following is *not* a role of entrepreneurs in the U.S. economy?
 - a. supply goods and services to meet consumer needs and wants
 - b. provide capital investment and job creation
 - c. determine how to allocate natural resources
 - d. serve as agents for change

17. Another name for economic resources is
 - a. factors of production
 - b. goods and services
 - c. supply and demand
 - d. command and market
18. The four basic principles of the U.S. economic system are
 - a. private property, freedom of choice, loss, competition
 - b. taxed property, freedom of choice, profit, competition
 - c. private property, freedom of choice, profit, competition
 - d. private property, limited choice, profit, competition
19. Which of the following is *not* a function of business?
 - a. production
 - b. marketing
 - c. legal environment
 - d. finance
20. If you were going to start a small retail store selling gift items, which type of market structure would you most likely be entering?
 - a. perfect competition
 - b. monopolistic competition
 - c. oligopoly
 - d. monopoly
21. The Ford Motor Company operates in which type of market structure?
 - a. perfect competition
 - b. monopolistic competition
 - c. oligopoly
 - d. monopoly

APPLY WHAT YOU LEARNED

22. You plan to start a pet-sitting/dog-walking business. Analyze the possible demand for such a service by brainstorming answers to the following questions: Who is likely to hire a pet sitter? Who is likely to hire a dog walker? Besides caring for the pets, what other services could such a business perform? Discuss what other questions you should consider before starting this type of business.
23. Susan Tran of Nails by Susan wants to increase her sales. Susan thinks about keeping the nail salon open two extra hours every day. She estimates that during the last two hours of every day, she and her staff could provide nail services to five more customers, bringing in additional revenues averaging \$125 a night. Susan estimates that providing the services to five more customers each night would cost approximately \$25 in supplies. Her operating expenses for electricity and water will increase by approximately \$20 per night. She would also have to pay two employees to work the extra two hours at a cost of \$30 each. What is the marginal benefit of keeping the nail salon open an extra two hours a day? What is the marginal cost of staying open two additional hours? Do you think Nails by Susan should stay open two extra hours each day?

MAKE ACADEMIC CONNECTIONS



24. **MATH** You have a business baking and selling chocolate chip cookies. Using the Activity CD, open the activity “How Much Does It Cost?” Print a copy and complete the activity. What are the costs of doing business? Are these fixed costs or variable costs?

25. **COMMUNICATION** Marketing plays an important role as one of the functions of business. Research and write a report explaining how each of the other functions—production, management, and finance—depends on the marketing function. Present your report to the class.
26. **ECONOMICS** Identify and research economies in the process of converting from a command to market economy. What events led to this change? What involvement, if any, do U.S. companies have in these countries' economies? Discuss your findings with the class.

WHAT WOULD YOU DO?

You are excited when you receive your new iPod for your birthday. You also receive a \$50 iTunes gift card. You sign onto iTunes and download many of your favorite songs and a movie. You spend the \$50 quickly, but there are many additional songs you want. One of your computer-savvy friends tells you about some web sites where you can download all the music you want for free. You are anxious to try out these new web sites, but you decide to talk to your parents first. Your parents explain that iTunes is a legal site and that the music artists receive royalties (payments to the copyright holder) when you download from it. The web sites your friend told you about do not give the artists the royalties due to them. Your friend says the artists have already made enough money so it does not really matter that you are getting the music for free. What will you do? Will you continue to pay and use only iTunes or will you use the free web sites? Why? Recording artists are entrepreneurs. If you were an entrepreneur, how would you feel if you did not get the money that was owed to you?

BUILD YOUR Business Plan *Project*

1. Using the Activity CD, open the activity "Supply and Demand Graph." Print a copy and complete the activity for at least one good or service your business will provide. Then use the graph to determine the price to charge for that good or service.
2. Determine the fixed and variable costs for your business. Estimate how much money you will need to cover these costs. Make a chart showing these expenses. Do you need to adjust your original pricing for your business to make a profit?
3. Consider adding another product or service to your business. What are the marginal costs and benefits of adding this new product or service? Is it a good or bad idea to add the item?



Planning a Career in Property Management



*Business, Management
& Administration*

"Our softball coach threw an end of season party for team members and their families at the pool in his neighborhood. There are about 300 houses in the neighborhood. A pool, playground, tennis courts, and clubhouse are shared and maintained by the community. He said that although the community elected a board of residents to plan for the community, the day-to-day maintenance of the community was handled by a property management company."

Who changes the light bulbs in the common areas of private communities? How is the landscaping of common areas managed in private communities? Who takes care of routine maintenance at retail sites?

Property management companies assist a variety of businesses by managing their daily operations. Retail locations, office parks, and residential communities use their services.

EMPLOYMENT OUTLOOK

- Average job growth is expected.
- Over half of property managers are self-employed.
- As new home developments form neighborhood associations to manage common areas, the need for property managers should increase.

JOB TITLES

- Assistant Facility Manager
- Commercial Property Assistant
- Occupancy Specialist
- Homeowners Association Field Manager
- Community Association Manager
- Portfolio Manager—Property Management

NEEDED SKILLS

- A Bachelor's degree is recommended.
- Strong information systems, financial, problem-solving, and multitasking skills are required.
- A background in real estate or facilities management is helpful.

What's it like to work in Property Management?

Ari, the owner of a property management company, was posting the minutes of a neighborhood's annual meeting on the neighborhood's web site. Web site maintenance was just one of the many services the neighborhood had hired Ari's company to perform.

Ari's next task was analyzing the bids that came in for the landscaping contract for a condominium community he was managing. He would prepare a report on the three most competitive bids and present them to the condominium's board tomorrow evening at their monthly meeting. In addition to providing a financial summary of the bids, Ari would also provide information regarding the reliability of the various landscaping companies. Because he managed several communities, Ari was able to obtain feedback on the effectiveness of a variety of landscaping companies.

After lunch, Ari reviewed the time cards for the lifeguards at a neighborhood community pool. Because the neighborhood lacked the resources to manage employees, they paid Ari's firm to handle the contract for their community's lifeguards.

What about you? Would you like to manage the day-to-day operations of a variety of communities to help them run smoothly?



EMERGING BUSINESS ISSUES EVENT

The Emerging Business Issues Event provides students with an opportunity to research and present an emerging business issue. The event will be completed by a team consisting of two or three members.

FBLA provides participants a topic to research. The team must then present an affirmative or negative argument about the topic, based upon random selection. Facts and working data should be secured from reliable sources. After drawing an affirmative or a negative argument, teams will have five minutes to finalize their preparations. Each presentation will last no longer than five minutes. Following each oral presentation, the judges have three minutes to ask questions.

TOPIC Closing the border with Mexico has become a heated political issue for the United States. Construction, manufacturing, agriculture, and horticulture are a few of the industries that depend heavily on illegal immigrants to fulfill labor needs. Some citizens and politicians want the country to shut down the border and deport illegal immigrants. Other individuals want the government to grant the current illegal immigrants a worker's permit and develop a strategy to enable them to become legal citizens. One plan recommends granting citizenship to more than 12 million illegal immigrants before tightening up the border. Other plans call for fining businesses that hire illegal immigrants. Your team will be called upon to argue the affirmative (granting illegal residents work permits and citizenship) or the negative (fine employers and send illegal residents home).

PERFORMANCE INDICATORS EVALUATED

- Understand how a current issue affects the economy.
- Communicate an opinion based upon facts and figures.
- Work as a team to persuade the audience to support a certain viewpoint.
- Manage time effectively to research, outline, and present a viewpoint.
- Demonstrate effective teamwork and align ideas into a persuasive argument.

Go to the FBLA web site for more detailed information.

Think Critically

1. What are two advantages of allowing illegal immigrants to stay in the United States?
2. Why are businesses concerned about the government's actions involving illegal immigrants from Mexico?
3. Why are politicians conflicted by the illegal immigrant issue?
4. How can the United States ensure that illegal immigrants take the necessary steps to obtain legal citizenship?

www.fbla.org

Chapter 3

© Digital Vision



Develop a Business Plan

3.1 Why a Business Plan Is Important

3.2 What Goes into a Business Plan?

3.3 How to Create an Effective Business Plan

school.cengage.com/entrepreneur/ideas

IDEAS IN ACTION

Turning an Idea into a Business

If you have an idea for a business, what do you do next? How can you raise money to get started? As Jeffrey Rodriguez and John Serrano of Brooklyn, New York, found out, a business plan is necessary to turn your idea into action.

Using their business plan, Jeffrey and John turned graffiti from an act of vandalism into an art form. John developed a love of art from an early age working with his artist father. Jeffrey developed leadership skills through the Boy Scouts and ASPIRA, a leadership club encouraging students to take part in community service in Latin neighborhoods. Both John and Jeffrey experimented with graffiti art, and Jeffrey started airbrushing designs for friends, working from a family-owned business using equipment borrowed from a Scout leader. After he taught John how to airbrush, Latin Artist was born.

Needing startup money, Jeffrey learned about Youth Venture, a program that awards grants to teens who start businesses emphasizing community service. Realizing that neighborhood youth needed a safe place to meet, Jeffrey applied for and got the grant. He and John used the money to fix up their store. They added a community service component to their airbrush designs business, offering free art lessons for neighborhood youth. Besides teaching them art, Jeffrey stresses the need to do something good for the community.

Four months after they opened, Jeffrey created a business plan and entered a Fleet Bank contest. Latin Artist was named one of the top 20 youth businesses in the New York area. Jeffrey and John continue to work on a detailed business plan so they can apply for a bank loan and determine the future direction of their business. A detailed business plan is a must when talking to banks and other lending institutions.

1. **Character** Are you honest and dependable?
2. **Capacity** Can you earn enough money to pay back the loan?
3. **Capital** Do you have enough cash on hand to pay your bills?
4. **Collateral** Do you have anything of value to back up your loan?
5. **Conditions** Do you have the potential to continue earning money?

What do you know?

1. What kind of plans do you think someone should make before opening a business?
2. Where could you go to research a business idea?
3. Why is it important to have a written business plan?



Jeffrey Rodriguez and John Serrano,
Latin Artist

© John Serrano (l.) and Jeffrey Rodriguez (r.)

3.1

Why a Business Plan Is Important

Goals

- Explain the purpose of writing a good business plan.
- Describe the importance of a business plan.

Terms

- business plan

Focus on Small Business

Look before you leap

Tony worked for a local automobile dealership as a technician for over 20 years. He was the best technician at the dealership, and he always received very high customer service ratings. One day, Tony decided that because he was such a good technician, he could make more money working on his own. At a local print and signage shop, he had business cards printed and a sign made that read "Tony the Technician." He quit his job at the dealer on Friday, put his sign up on Sunday, and was open for business on Monday.

Work as a Team Tony made his decision very fast and jumped right into owning his own business. What do you think are Tony's chances for success? Discuss what advice you would have given Tony if he had talked to you about his idea first.



© Getty Images/PhotoDisc

Planning is the key when starting a business.

The Business Plan

Once you have settled on a business idea, it is time to start making plans for the business. A **business plan** is a written document that describes all the steps necessary for opening and operating a successful business. In this chapter, you will learn what goes into a business plan and begin the development of a business plan for your business idea.

A business plan does the following:

- Describes what your business will produce, how you will produce it, and who will buy your product or service
- Explains who will run your business and who will supply it with goods
- States how your business will win over customers from competitors and what your business will do to keep customers



© Digital Vision

Why would potential investors want to see your business plan?

- Provides detailed financial information that shows how your business will succeed in earning a profit

Writing a business plan is one of the most difficult and important things you will do as an entrepreneur. Writing a solid business plan is critical because the plan can make or break your business. Some people may tell you that you do not really need a business plan, but potential investors will want to know in what you are asking them to invest. The business plan will also serve as a guide for you as you get your business started.

Purposes of a Business Plan

The business plan serves three important purposes.

1. **A business plan explains the idea behind your business and spells out how your product or service will be produced and sold.** To convince investors that your business idea is solid, you will need a completely new product or service or one that is better or less expensive than products or services that already exist. You will need to identify your target customer and show how your company will be able to obtain and keep customers.
2. **A business plan sets specific objectives and describes how your business expects to achieve them.** A good business plan includes sales projections for the short term (the first year), the medium term (two to five years after startup), and the long term (five years in the future). It describes what products and services will be introduced over the next five years and sets forth future business plans, such as expansion of the business.
3. **A business plan describes the backgrounds and experience of the people who will be running the business.** Banks and investors make financing decisions based on how well they think

★ Develop Your Reading Skills

As you read this chapter, make a list of the items that you will need to develop and research for your business plan.



a company can meet its objectives. By providing the background and experience of the people who will be running your company, the bank or investor will be more likely to provide funding.

Checkpoint

What are the three main purposes of a business plan?

Importance of a Business Plan

Every new business must have a business plan. The business plan is important for several reasons.

1. **A business plan makes you think about all aspects of your business.** It will help you during the development and startup phases of the business. Stan Meyer began a graphic design business from his home. He spent many hours thinking about the business and thought he was ready to start it until he sat down to write his business plan. He had not made sales and profit projections. He had also not thought about the possibility that he might need to hire staff if the business grew too large for him to handle alone. Drafting a business plan helped Stan gain even more confidence in his business idea. It showed him that building a successful business based on his concept would be possible. Working on his business plan also helped Stan think through business strategies, recognize limits, and identify problems he might encounter.
2. **A business plan may help you secure financing for your business.** You may have a great idea, but very little capital to invest in your business. You may need to go to a bank to obtain a loan



© Digital Vision

How does creating a business plan help you see the "big picture"?

or find other investors for your startup money. Lenders and investors require a business plan before they will consider financing a business. A well-written business plan shows lenders and investors that you are serious about your business idea and have spent sufficient time in the planning process. The loan officer at Stan Meyer's bank was very impressed with the work that Stan had put into his business plan. The plan showed her that Stan thoroughly understood all that was involved in starting his own graphic design business. She recommended that he be approved for a loan.

3. A business plan helps you communicate your ideas to others.

By the time you write your business plan, you will have given much thought to the business you want to establish. You will proceed believing that your business can succeed. If you communicate your ideas well on paper, you will also convince the readers that your business can succeed. It will give suppliers confidence in

Famous Entrepreneur

Walter Elias Disney

No one has entertained families more than the Walt Disney Corporation. Who has not experienced the Disney brand by seeing a movie, visiting a theme park, staying at a resort, buying merchandise, watching TV, or cheering on the Mighty Ducks of ice hockey? We have all been touched by the magic of Disney, the preeminent name in family entertainment.

As a young child, Walt Disney had an interest in art. To improve his drawing skills, he took art courses in high school, and at night, attended the Academy of Fine Arts. The humble beginnings of his colossal corporation date back to 1923 when Walt arrived in California to peddle one of the cartoons he had made. Although the cartoon was not an initial success, Walt did not give up. He started working with his brother, Roy, in his uncle's garage. Success did not come quickly to the Disney brothers, but Walt's faith in himself and others helped him to succeed.

Mickey Mouse was created in 1928. Mickey made his screen debut in the world's first fully synchronized sound cartoon, *Steamboat Willie*. In the midst of the Great Depression of the 1930s, Disney took great risk and invested a then-unheard-of amount of \$1.5 million to produce the first full-length animated musical feature, *Snow White and the Seven Dwarfs*.

Disney began television production in 1954 and was among the first to present full-color programming with his *Wonderful World of Color* in 1961. Disney opened the first of many theme parks in 1955. The Disney Corporation continues with innovation and success today.

Think Critically

Do you think success comes quickly for most entrepreneurs? What do you think Walt Disney's first business plan included as his vision for the company?



Why do you think Walt Disney was a successful entrepreneur?

extending credit to your company. Stan presented his business plan when he visited the local office supply company. With it, he convinced the company to sell him a computer system on credit.

4. A business plan can serve as a tool for managing your business.

Once your business is up and running, you can use the business plan in your decision making. Stan Meyer regularly uses his business plan to help him manage his company, Designs for You. Stan's plan laid out his vision of how the company would grow over time. By following the strategies in his plan, he has increased sales by offering innovative designs and reaching new clients.

Checkpoint

Why is a business plan important to an entrepreneur?

3.1 Assessment

THINK ABOUT IT

1. Why do you think the quality of the business plan is so critical to an entrepreneur's success?
2. Melinda Rosati wants to purchase her uncle's barber shop. Because it is an ongoing business, Melinda doesn't think she needs to write a business plan. Do you agree or disagree with Melinda's opinion? Why or why not?
3. Putting your business plan in writing helps you communicate your ideas to others. Do you think discussing your business plan out loud in a meeting can also help get your ideas across? Why or why not?

MAKE ACADEMIC CONNECTIONS

4. **MANAGEMENT** André Kitaevich uses the business plan he wrote to help him run day-to-day operations in his jewelry store. On what specific issues might André consult his plan?
5. **COMMUNICATION** You are starting a business in the home healthcare field. Write a paragraph explaining the idea behind the business. Be sure to spell out how you plan to market its services.



TEAMWORK

Working in a team, choose a well-known business in operation today. Research the history of the business. Find out who started the business, why the person had the idea to start the business, and when the business was started. Prepare a presentation for your class about the history of the business.

3.2

What Goes into a Business Plan?

Goals

- List and describe the basic elements of a business plan.
- Describe how to pull a business plan together.

Terms

- pro forma financial statement
- cover letter
- statement of purpose
- executive summary

Focus on Small Business

Create interest in your business plan

Having always had a strong interest in electronics and computers, Andy wanted to start a business building customized computers for business and personal use. He knew that he would need about \$5,000 to get his business started. He had \$2,000 in savings that he could use, but he was going to have to get a loan from family, friends, or the bank for the remaining \$3,000. He sat down one night and threw together a few facts about his business and handwrote a list of items that he needed to purchase. The cost of the items on the list totaled \$1,950. He showed the information he had compiled to his parents, his grandparents, his aunt and uncle, and his friend. No one was interested in making an investment in his business.

Work as a Team Discuss why you think Andy could not interest anyone in making an investment in his business. How do you think a formal business plan would improve his chances of finding lenders?



© Getty Images/PhotoDisc

A formal business plan is the best way to share your business idea.

Basic Elements of a Business Plan

Every new business should have a business plan, but not all business plans are alike. The content of a business plan for a small, home-based, single-owner business will differ from a business plan for a large corporation with offices in many cities. But regardless of the business, all business plans serve the same basic purposes. They should also contain the same three basic components—introductory elements, the main body, and the appendix.

The main body of the business plan will contain the bulk of the information about the business idea. It provides details on how the business will succeed. A lot of time and effort will go into writing the



© Getty Images/PhotoDisc

What kinds of information do you think investors would want to know about a new day care center?

main body of the plan, and it should be compiled before the other components in the business plan. It should be organized into the following sections, or elements:

1. Introduction
2. Marketing
3. Financial Management
4. Operations
5. Concluding Statement

Nora Ellis and Samantha Richards are qualified child-care providers who have worked together at a day care center for many years. Because of the high demand for quality day care services, Nora and Samantha know they are well positioned to meet this need. They decide to create a business plan for opening their own center.

Introduction

The introduction section of a business plan contains many important details about the proposed business idea. The following information should be included in the introduction section.

- A detailed description of the business and its goals
- The ownership of the business and the legal structure
- The skills and experience you bring to the business
- The advantages you and your business have over your competitors

DETAILED DESCRIPTION Something inspired the idea for your business. Describing how you came up with your idea can help lenders, investors, and others understand what your business is about. Your business plan should also outline your short-term (three months to one year), medium-term (two to five years), and long-term (more than five years) goals. This section describes your vision for the company's future. Stating goals will help provide you with direction and focus for your business activities.

Nora and Samantha know their short- and medium-term goals. In the first year of business, they want to get financing to lease or buy a facility, equip the facility, and staff it. By their third year of business, they want to invest in more equipment and expand their facility. They have not yet thought through what their objectives are for the long term. Writing a business plan will force them to think about future plans.

OWNERSHIP AND LEGAL STRUCTURE In your business, you should have a section detailing your form of ownership. Will it be a sole proprietorship (one owner), a partnership (two or more owners), or a corporation (many owners that hold shares of stock in the business)? Provide information relevant to your form of business, such as who your partners are or how many shareholders you have. This section of the business plan is important because each legal form of business has an effect on how the business works and makes profits.

SKILLS AND EXPERIENCE A written summary of your experience is an essential part of your business plan. This summary should emphasize all experience you have that relates to the business, including paid work experience, volunteer experience, and any hobbies you have that relate to your proposed business. The skills and experience of any managers or professional employees who will be hired will also be relevant.

Nora and Samantha have Master's degrees in early childhood education. Together, they have more than 35 years of experience in day care, including 15 years in management. To show that they are well qualified to run a center, they include copies of their resumes and letters of reference from satisfied parents.

ADVANTAGES You should list your company's advantages over the competition. These advantages may include the following:

- Performance
- Quality
- Reliability
- Distribution
- Price
- Promotion
- Public image or reputation

Marketing

The marketing section of your business plan should describe the products and/or services you will offer, the market, the industry, and your location. Developing a marketing plan will be examined in more detail in Chapter 5.

PRODUCTS/SERVICES Describe your products and services and explain how they differ from those already on the market. Highlight any unique features, and explain the benefits customers will receive by purchasing from your business.

MARKET You will explain whom your prospective customers are, how large the market is for your product or service, and how you plan to enter that market. You should also explain how you plan to deal with competition.

INDUSTRY You should describe the industry in which you will operate. To find this information, you will need to perform research. Things you should include in this section are as follows:

- External factors affecting your business, such as high competition or a lack of certain suppliers
- Growth potential of the industry, including growth forecasts
- Economic trends of the industry
- Technology trends that may affect the industry

LOCATION Describe the location of your business. Lenders and investors want to know exactly where your business will be, because the location of a business is often a critical factor to its success.



Writing the marketing section of the business plan is easy for Nora and Samantha, because they have a clear idea of what they want to do. Their prospective customers are the parents of the 1,000 to 1,500 children between the ages of two and five who live in their area. Nora and Samantha determine that 90 percent of the families would be able to afford their center. They will advertise in local newspapers and send out fliers to families in their target market. When providing information on the industry in which they will operate, they include population data for their area. This information shows that demand for their service could grow over time. Nora and Samantha describe their plan to start the business in a prime location, in the heart of a suburb where most families have young children and both parents work outside the home.

Financial Management

The financial section of your business plan will help determine your financial needs. It forces you to look at financial risks and the costs and expenses of running your business. It consists of three elements.

WHAT WENT WRONG ?

Do Market Research

While working as a salesperson for a custom exhibit display company, Leo Hunt found a unique product not currently being marketed in the United States. It was a lightweight, portable, full-color display that could be set up and dismantled quickly. A company in Sweden was the manufacturer of this display. Leo thought it was ideal for trade shows and conventions. Leo decided to become a distributor of the special displays. He quickly prepared a business plan focusing on the unique features of the product and the fact that there was no competition in the United States for the product. He estimated that he could generate over 5,000 sales in the first quarter of the year. He did very little research and assumed that everyone who exhibited at a trade show would be part of his target market. He placed a large order with the manufacturer and was ready to go! Within three months, Leo had taken only 250 orders for the product, had spent 95 percent of his startup capital, and found that many exhibitors had no need for his product. After six months, Leo had bills piling up, fewer than 100 orders,

an overdrawn checking account, and some very unhappy employees. Leo decided it was best for him to close his business.

Think Critically

1. What mistakes did Leo make when preparing his business plan?
2. Do you think Leo should have ordered displays from the manufacturer before he had orders from customers?
3. Are there steps Leo could have taken to try to save his business?



© ScottOlson/Getty Images

Market research is critical to the success of a business.

- 1. Identification of Risks** Prospective lenders and investors will want to know what risks your business faces and how you plan to deal with them. Do not be afraid to list potential problems. Lenders know that every business faces risks. They will be reassured to see that you have clearly thought through the potential problems and have a plan for dealing with them. Risks typically faced by new businesses include competitors cutting prices, costs exceeding projections, and demand for your product or service declining.
- 2. Financial Statements** A new business must include projected financial statements in its business plan. An existing business must include current as well as projected statements. A financial statement based on projected revenues and expenses is called a **pro forma financial statement**.
- 3. Funding Request and Return on Investment** You must indicate how much you need to borrow and how you plan to use the money. You should give investors an idea of how much money they could expect to earn on their investment in your business. You should state how much money you are personally investing and provide a personal financial statement.

Nora and Samantha have included pro forma financial statements for their business, which show how much money and profit they expect to earn. They require \$140,000 to start their business. Together they are contributing \$85,000 of their own money. This means they need a bank to loan them \$55,000. They include this information in their plan as well.

Operations

The operation of your company is critical to its success. In this section of your business plan, you should explain how the business will be managed on a day-to-day basis and discuss hiring and personnel procedures. You should also include information on insurance and lease or rental agreements. Describe the equipment that will be necessary for production of your products or services and how the products or services will be produced and delivered.

As part of the operations section of their business plan, Nora and Samantha describe hiring plans to ensure their day care center is well-staffed. They also devote a section to health and safety and outline plans for dealing with emergencies.

Concluding Statement

In this section, you should summarize the goals and objectives you have for your business. You should also emphasize your commitment to the success of the business.

Checkpoint

List the elements of the main body of a business plan and explain why each one is important.



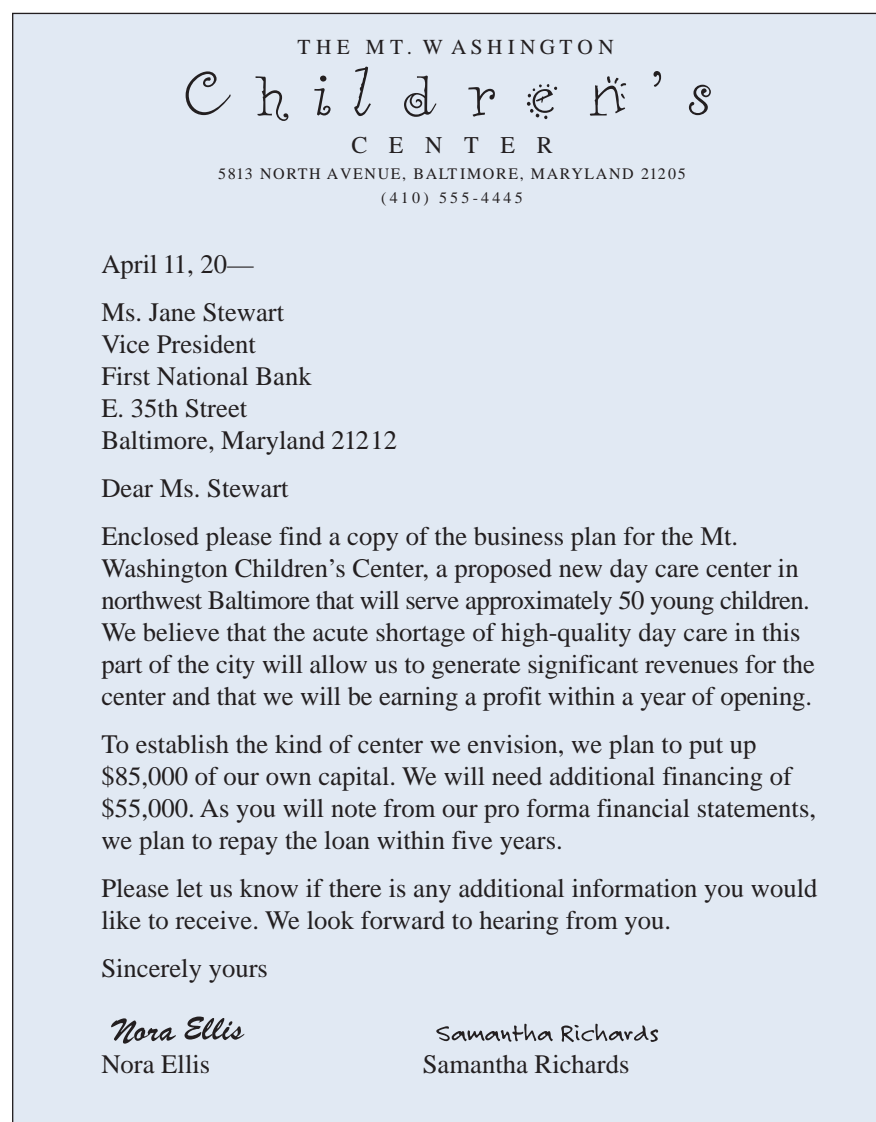
Complete the Business Plan

After you have completed the main body of your business plan, you will need to focus your efforts on the other components—the introductory elements and the appendix. Then you must pull all the components together into a well-organized, attractive document.

Introductory Elements

Every business plan should begin with a cover letter, a title page, a table of contents, a statement of purpose, and an executive summary. These elements help set the tone for the body of your business plan.

COVER LETTER A letter that introduces and explains an accompanying document or set of documents is called a **cover letter**. The cover letter for your business plan should include your name, the name of your business, and your address and telephone number. It should briefly describe your business and its potential for success. It also needs to tell the reader how much capital you need. Nora and Samantha prepare the cover letter shown below.



TITLE PAGE Your business plan should have a title page that indicates the name of your company, the date, the owner of the company, the title of the owner, and the address and phone number of the company.

TABLE OF CONTENTS A table of contents is a listing of the material included in a publication. It shows the reader what each page covers. It is similar to a table of contents in a textbook. It is important that your table of contents is accurate, so make sure the sections are listed in the proper order and the given page numbers are correct.

STATEMENT OF PURPOSE A brief explanation of why you are asking for a loan and what you plan to do with the money is called a **statement of purpose**. It should be no more than one or two paragraphs. Nora and Samantha write the statement of purpose shown here.

EXECUTIVE SUMMARY Before getting into the detail of the main body of the business plan, readers will want to read an executive summary. An **executive summary** is a short restatement of the report. It should capture the interest of its readers and make them want to read more. If the executive summary is unconvincing, a lender may decide not to read your entire business plan. This makes a strong executive summary critical to the success of your business.

The executive summary should be no longer than one or two pages, and it should be written in a clear, simple style. Your executive summary should do all of the following:

- Describe your business concept and communicate what is unique about your idea
- Include your projections for sales, costs, and profits
- Identify your needs (inventory, land, building, equipment, etc.)
- State the amount you are interested in borrowing

STATEMENT OF PURPOSE

The Mt. Washington Children's Center will operate as a private day care center serving approximately 50 children in northwest Baltimore. The Center will offer excellent supervision in a clean, safe, and intellectually stimulating environment.

The project is requesting \$55,000 in financing. This money will be used to:

- rent and remodel 4,000 square feet of indoor space
- prepare 18,000 square feet of outdoor space for use as a playground
- purchase equipment such as swings, jungle gyms, sand-boxes, and supplies
- pay salaries of eight employees until sufficient cash flow is generated to allow operating expenses to be covered

EXECUTIVE SUMMARY

The Mt. Washington Children's Center (MWCC) will be established as a partnership in Baltimore, Maryland. It will be owned and operated by Nora Ellis and Samantha Richards, highly respected child-care professionals with more than 35 years of experience in the field. Three experienced teachers and three teacher aides will supervise approximately 50 boys and girls between the ages of 2 and 5. In addition, a receptionist/bookkeeper and a cleaning/maintenance person will be hired.

MWCC is being established in response to the shortage of high-quality child care in northwest Baltimore. Only two small day care centers now serve a population of 45,000 upper-middle-class professionals. In 75 percent of these households, both parents work outside the home. The accessible location of the Center will make it an extremely attractive day care option for parents in the area. When completed, its facilities, which will include four large outdoor play structures and eight personal computers, will represent state-of-the-art day care. Its staff will comprise the finest day-care professionals in Baltimore, led by a management team that is recognized throughout the region.

Market research indicates that the MWCC could expect to fill 90 to 100 percent of its student positions immediately upon opening and that the center would be profitable as early as the third year of operation. Expansion could begin in the third year. To finance the startup of the company, its owners are seeking \$55,000 in financing, which they would expect to repay within five years.





© Purestock

Why do you think lenders and investors read the executive summary first?

Although the executive summary appears before the body of the business plan, it should be written *after* the business plan has been completed. To write the executive summary, go through the business plan and find the most important and persuasive points you have made. Then draft an outline of an executive summary based on these points.

Once you have created a draft of your executive summary, ask people who do and do not understand your business to read the summary. If readers do not come away with a clear sense of what you plan to do and why you will succeed in doing it, your executive summary needs more work. Nora and Samantha's executive summary is shown on the previous page.

Appendix

The appendix to the business plan includes supporting documents that provide additional information and back up statements made in the body of the report. To help you determine what supporting documents to include, you should ask yourself what you would want to know about a business before you would lend it money. Documents that might be included in the appendix include the following:

- Tax returns of the business owner for the past three years
- Personal financial statement of the owner
- Copy of proposed lease or purchase agreement for the building space
- Copy of licenses and other legal documents
- Copy of resume of the owner
- Letters of recommendation
- Copies of letters of intent from suppliers
- Copies of any large sales contracts you have already negotiated



Put It All Together

Your business plan is your best opportunity to let other people know what you want to do with your company. It gives you the chance to convince them that your idea is sound and that you have the talent and resources to make your idea a successful business venture. To make the best of this opportunity, you will want to create an attractive document that is neat, well organized, and inviting to read. Handwritten business plans are not acceptable. All business plans must be word processed and printed on standard-sized white paper. In addition, your business plan should follow a standard format containing the introductory elements, the main body, and the appendix.

Checkpoint

Why should you include supporting documents in your business plan?

3.2 Assessment

THINK ABOUT IT

1. Why is it possible to write an executive summary only after you have written the main body of your business plan? Why might the executive summary be more important than the body of the plan?
2. Why do you think it is important to include management and staffing issues in the operations section of your business plan?
3. A group of investors is planning to open a new amusement park. What supporting documents will need to be included in their business plan?

MAKE ACADEMIC CONNECTIONS

4. **MATH** You plan to start a corporation. You have \$67,500 in savings, but need \$165,000 total to begin your business. How much money will you need from investors? What will be your percentage of ownership? If you have four outside investors, how much will each investor need to invest? What percentage will each investor own?
5. **COMMUNICATION** Write short-, medium-, and long-term goals for an entrepreneur starting a new ice cream parlor.



TEAMWORK

Working with team members, choose a business in your local community. Make a list of the items you think this business would include in each component of its business plan—introductory elements, main body, and appendix.



3.3

How to Create an Effective Business Plan

Goals

- Describe resources available for researching your business plan.
- Name common mistakes to avoid in business planning.

Terms

- Small Business Administration (SBA)
- Small Business Development Centers (SBDC)
- Service Corps of Retired Executives (SCORE)
- trade associations

Focus on Small Business

Where do I start?

Michelle always loved working with children. All of the parents in her neighborhood wanted her to babysit for them. She was always thinking up fun games to play and creative activities for the children to do. She wondered if she could do even more with these activities to earn money for college. She talked with her mother and some of the parents and came up with an idea. She would run an ice cream parlor where she could host parties and let the children make their own ice cream sundaes, play games, and watch movies. Once Michelle came up with a business idea, she knew it was time to make a detailed plan. However, she did not really know how to get started on a plan.

Work as a Team What kind of information do you think Michelle needs to gather? Where might Michelle find this information and whom might she talk with to learn more about starting a business?



© PhotoDisc/Getty Images

Your interests and hobbies can lead to a new business.

Research the Business Plan

Your business plan needs to convince readers that you have come up with a practical business idea. To do this, you must include information and data from objective sources to show that your idea is founded on solid evidence. Researching and writing a business plan takes time. In fact, most entrepreneurs spend 50 to 100 hours developing their business plans. The process requires patience, research, thought, and a great deal of writing and editing.

Pulling together the information you need for your business plan involves researching your business, from leasing space or equipment to what you will charge for your product or service to dealing with competitors. Researching will teach you a great deal about running a business and may provide you with specific ideas for starting a company.

Community, Government, and Professional Resources

When writing a business plan, you will likely need to seek out advice from others. People from many organizations can help you with your business plan. Available resources include the SBA, the SBDC, SCORE, your local chamber of commerce, trade associations, and professional business consultants.

THE SBA The U.S. **Small Business Administration (SBA)** is an independent agency of the federal government that was created to help Americans start, build, and grow businesses. The SBA also provides aid, counsel, and assistance to protect the interests of small business concerns, to preserve free competitive enterprise, and to maintain and strengthen the overall economy of our nation.

THE SBDC The Office of **Small Business Development Centers (SBDC)** provides management assistance to current and prospective small business owners. Counselors from the SBDC provide free one-on-one assistance in developing a business plan. They also provide inexpensive workshops on topics that may help you develop your plan. SBDCs have many resources in one place to assist individuals and small businesses. SBDCs were formed as a cooperative effort of the private sector, the educational community, and federal, state, and local governments. They enhance economic development by providing small businesses with training and technical assistance. Assistance from an SBDC is available to anyone who cannot afford the services of a private consultant and who is interested in beginning a small business for the first time or improving or expanding an existing small business.

SCORE Another source of valuable assistance is SCORE. The **Service Corps of Retired Executives (SCORE)** is made up of more than 10,500 retired executives who volunteer their time to provide entrepreneurs with real-world advice and know-how. They provide free confidential advice that could be helpful to you as you prepare your business plan. You can set up a meeting with a SCORE volunteer, or you can work with a SCORE volunteer over the Internet. SCORE also offers workshops that are a valuable way to learn more about doing business and a way to network with other business professionals who can help you succeed. The topics of the workshops focus on important small business issues, ranging from business planning and marketing to Web-based retailing. The SCORE counselors represent every business area. Some have worked as executives at Fortune 500 companies, while others were small business owners themselves. SCORE can provide assistance for you for just a few sessions or a number of years, based on your needs.

did you KNOW?

Since 1964, 7.5 million entrepreneurs have been counseled by SCORE or attended SCORE workshops.



Why is it a good idea to seek the help and advice of others when writing a business plan?

© Digital Vision

BE YOUR OWN BOSS

You want to start a plant nursery. You have taken horticulture classes in school and want to find a way to turn your acquired knowledge and love of plants into a profitable business. You start working on your business plan and realize that you need help. You decide to contact the Service Corps of Retired Executives (SCORE) for assistance.

Prepare for your first meeting with the SCORE volunteer. Write a brief summary explaining your business idea, why you want to start the business, and what you hope to accomplish by starting the business. Compile a list of questions you want to ask the SCORE volunteer.

CHAMBER OF COMMERCE In many communities, the local Chamber of Commerce offers assistance and information to entrepreneurs. It can provide information on trends affecting local businesses, local resources, and zoning and licensing information.

TRADE ASSOCIATIONS Organizations made up of professionals in a specific industry are called **trade associations**. They exist to provide information, education, and networking opportunities to individuals in their industry. These associations can be valuable sources of information to entrepreneurs.

PROFESSIONAL CONSULTANTS Some entrepreneurs hire experts to help them. Professional business consultants can be found in directories available in your library or on the Internet.

FINANCIAL INSTITUTIONS Many entrepreneurs are not familiar with the financial aspect of starting and running a business. When writing the financial section of your business plan, it may be beneficial to talk with a banker and an accountant. They can help answer your questions about loans and financial statements.

Print Resources

Information for your business plan can come from many print sources. Your public library will have many books on entrepreneurship that may provide you with valuable information on running your own business. In addition, books on marketing, financing, hiring and managing a staff, purchasing a business, and operating a franchise can be helpful. The library will also have books devoted specifically to writing a business plan that include sample business plans.

Magazines may also prove helpful—especially magazines devoted to small business ownership and to the industry in which you will be competing. Ask your librarian to help you find magazines that contain information that may be relevant to your business plan.

Government documents, including publications issued by the Small Business Administration (SBA) and other federal agencies, may provide you with useful information. The SBA district office nearest you will have many publications that can help you complete your business plan.

Online Resources

Much of the information you find in print resources is also available on the Internet. The SBA, SBDC, and SCORE web sites contain much of the same information that is provided in print. Many magazine articles that deal with entrepreneurial topics can be found online.



In addition, there are many sites specifically for entrepreneurs and small businesses that may give you detailed information. Internet search engines can help you locate resources.

Nora and Samantha, who are starting their own day care business, began research for their business plan by reading books from the library. They also read information on day care facilities that they received from the Small Business Administration. They found many samples of business plans on the Internet that they were able to adapt to meet their needs. Once they had an outline prepared for their business plan, they met with a counselor from their local Small Business Development Center to get feedback and advice for improving their business plan. The number of hours spent on research helped Nora and Samantha prepare an effective business plan.

NETBookmark

Plenty of teenagers have started their own businesses. The most successful teen entrepreneurs have prepared business plans just like adults. Access school.cengage.com/entrepreneur/ideas and click on the link for Chapter 3. Read the article, "Teen Entrepreneurs Vie for Seed Money." What did the teen entrepreneurs include in their business plans? What do you think would be the most difficult part of a business plan to develop? Why?

school.cengage.com/entrepreneur/ideas

Checkpoint

What are some of the resources that are available to help you develop your business plan?

Mistakes in Business Planning

Many entrepreneurs will not take the necessary time to carefully plan their business and prepare their business plan. This can contribute to difficulties in getting their business started as well as business failure.

To create an effective business plan, avoid making the following common mistakes:

1. **Unrealistic Financial Projections** Many investors will go straight to the financial section of the business plan, so it is very important for the projections in this section to be realistic. Projections should be based on solid evidence for the potential growth of the company.
2. **An Undefined Target Market** You must clearly define your market and give a clear picture of your potential customers. Clearly explain why these customers will buy your product. Be realistic about your market and do not assume that everyone will want to buy your product or service.
3. **Poor Research** Many potential business owners are anxious to get their business operating and do not spend the time necessary to do good research. Use up-to-date research information, and verify the facts and figures in your business plan.



4. **Ignored Competition** Do not overlook the competition and do not focus only on what the competition has done wrong. Investors want to see who your competition is and how you plan to compete in the market. Outline how you will differentiate yourself from the competition.
5. **Inconsistencies in the Business Plan** It is important to review your final business plan and be sure that your plan is well written and formatted in an attractive style. Be sure that information provided is consistent from section to section. It is a good idea to have an objective person review your final business plan before you show it to investors.

Checkpoint

List some common mistakes that are made in business planning.

3.3 Assessment

THINK ABOUT IT



1. When writing a business plan, it is important to consider all of the resources available to help you through this process. Using the Activity CD, open the activity "Business Plan Resources." Print a copy and complete the activity.
2. Some elements of the business plan require outside source information. If your business manufactures cardboard boxes, what specific sources might you need to consult?
3. Why is it important for financial projections to be as realistic and as accurate as possible when writing your business plan?

MAKE ACADEMIC CONNECTIONS

4. **LANGUAGE ARTS** Locate an article about entrepreneurship in the library or on the Internet. Write two paragraphs summarizing the main points of the article.
5. **MATH** If you intend to borrow 20 percent of the \$174,500 you need to start a business, how much of your own funds are you investing?



TEAMWORK



Working in a team, review a business plan that you obtained from the Internet or from a company in your community. Using the Activity CD, open the activity "Business Plan Review." Print a copy and complete the activity by listing the features that you think are effective and the features that need improvement. Make suggestions for improving the business plan.



Sharpen Your Entrepreneurial Skills

Using Technology Tools

There are many software programs available for entrepreneurs to use when preparing a business plan. A recent Internet search showed over 345,000 matches for “business plan software.” Many entrepreneurs use these programs because they provide an easy-to-use template. By plugging your specific information into the template, you get a professional-looking finished report. If you decide to use a software program to create your business plan, be sure it includes all of the essential elements. It is a good idea to evaluate several different programs before deciding which one to use. Your choice should best match the information you want to include and your desired style. And, of course, it should be one that you can use without difficulty.

TRY IT OUT

Using the Internet and advertisements from magazines and newspapers, find the names of at least three business plan software programs. Make a list of the features of each program and its cost. Evaluate the programs and decide which one you would select if you wanted to use a software program to prepare your business plan. Justify your decision.



© Tetra Images

Chapter 3 | Assessment

SUMMARY

3.1 Why a Business Plan Is Important

1. A business plan is a written document that describes all the steps necessary for opening and operating a successful business. It explains the idea behind your business and spells out how your product or service will be produced and sold. It sets specific objectives and describes how your business will achieve them. It describes the backgrounds and experiences of the people who will be running the business.
2. Writing a business plan is important because it makes you think about all aspects of your business, helps you secure financing for your business, helps you communicate your ideas to others, and can serve as a tool for managing your business.

3.2 What Goes into a Business Plan?

3. The main body of the business plan should include the following sections: Introduction, Marketing, Financial Management, Operations, and Concluding Statement.
4. To complete the business plan, you need to prepare introductory elements consisting of the cover letter, title page, table of contents, statement of purpose, and executive summary. The executive summary is the most important element and should not be written until the main body of the plan is complete. You also need to compile an appendix, which includes supporting documents that provide more information to the readers of the plan.

3.3 How to Create an Effective Business Plan

5. To show you have a practical business idea, you must include information and data from objective sources. People from many organizations—including the SBA, the SBDC, SCORE, your local chamber of commerce, trade associations, professional business consultants, and financial institutions—can help you with your business plan. Print resources can be obtained at the public library and through Government agencies. An extensive amount of information is also available on the Internet.
6. Common mistakes made in business planning include unrealistic financial projections, an undefined target market, poor research, ignored competition, and inconsistencies in the business plan.

What do you know now?

Read Ideas in Action on page 63 again. Then answer the questions a second time. How have your responses changed?

VOCABULARY BUILDER

Match each statement with the term that best defines it. Some terms may not be used.

1. A written document that describes all the steps necessary for opening and operating a successful business
2. A financial statement based on projected revenues and expenses
3. A letter that introduces and explains an accompanying document or set of documents
4. A short restatement of a report
5. A brief explanation of why you are asking for a loan and what you plan to do with the money
6. An independent agency of the federal government created to help Americans start, build, and grow businesses
7. Organizations made up of professionals in a specific industry
8. Organization made up of more than 10,500 retired executives who volunteer their time to provide entrepreneurs with real-world advice and know-how

- a. business plan
- b. cover letter
- c. executive summary
- d. pro forma financial statement
- e. Service Corps of Retired Executives (SCORE)
- f. Small Business Administration (SBA)
- g. Small Business Development Centers (SBDC)
- h. statement of purpose
- i. trade associations

REVIEW YOUR KNOWLEDGE

9. A business plan is *not* intended for
 - a. your competition
 - b. potential investors
 - c. your bank
 - d. any of the above
10. Purposes of a business plan include which of the following?
 - a. it explains your idea for a product or service
 - b. it sets specific objectives and describes how they will be achieved
 - c. it describes the backgrounds and experiences of the people who will run the business
 - d. all of the above
11. A business plan is important for a new business for all of the following reasons *except*
 - a. it makes you think about all aspects of your business
 - b. it can help you communicate your ideas to others
 - c. it guarantees you will get financing for your business
 - d. it can serve as a tool for managing your business
12. The main body of a business plan includes which of the following elements?
 - a. executive summary
 - b. statement of purpose
 - c. financial management
 - d. supporting documents
13. Which of the following is *not* a true statement regarding risks?
 - a. Identifying the possible risks your business faces will alarm lenders and investors and cause them to withhold funds.
 - b. Potential investors and lenders want to know what risks your business faces and how you plan to deal with them.
 - c. Lenders will appreciate the fact that you know what risks you face and have a plan for dealing with them.
 - d. Lenders know that every business faces risks.

14. The purpose of including supporting documents in a business plan is to
 - a. make the plan lengthy
 - b. provide additional information
 - c. give the readers more information than they might need
 - d. explain your business idea
15. Writing a business plan
 - a. is a quick and easy process
 - b. is quick but difficult
 - c. requires patience, research, thought, and time
 - d. none of the above
16. Which of the following organizations can provide assistance when writing your business plan?
 - a. bank
 - b. Chamber of Commerce
 - c. Small Business Development Center
 - d. all of the above
17. Which of the following describes why you are asking for a loan and what you plan to do with the money?
 - a. cover letter
 - b. statement of purpose
 - c. executive summary
 - d. title page
18. Mistakes to avoid when preparing your business plan include all *except*
 - a. providing unrealistic financial projections
 - b. wasting time on research
 - c. ignoring the competition
 - d. failing to define the target market

APPLY WHAT YOU LEARNED

19. Obtain a sample business plan. Review the business plan and discuss whether or not the five common mistakes in writing a business plan were avoided. Provide reasons to support your decisions.
20. You plan to open a skateboarding park. What kind of research should you do? What sources will you consult for your research?

MAKE ACADEMIC CONNECTIONS

21. **COMMUNICATION** You are preparing a business plan for a self-storage facility (U-Store-It). You are requesting a \$75,000 loan to buy the property and storage lockers. Write the cover letter to the bank loan officer and a statement of purpose.
22. **RESEARCH** Choose a business with which you are familiar. Using the Activity CD, open the activity “Trade Association Research.” Print a copy and complete the activity by using the Internet or the library to research trade associations that could provide useful information to the business.
23. **COMMUNICATION** An entrepreneur’s resume is an important supporting document for a business plan. It tells the reader about the entrepreneur’s qualifications for running the business. Research resume formats and choose one that you think would be suitable for you. Prepare a resume outlining your experience for running a business.



WHAT WOULD YOU DO?



You have a great idea for a business you want to start. Because you are going to school full time and work nights and weekends, you really do not have the necessary time to spend preparing a business plan. However, you know you need a business plan to help you secure a loan to get the business started. While searching the Internet, you find a business plan for a company that is very similar to the one you want to start. It would save you time if you copied this plan, changed the business name, and added your personal information. What would you do? What problems might this cause?

BUILD YOUR Business Plan Project

This activity will help you get started on the development of a business plan for your business idea.

1. Describe how you came up with the idea for your business project. Explain why there is a market/need for your product or service. Interview five or more people about your product or service. How many of them would buy it? Did any of them make suggestions? Prepare a one-page report that fully describes your product or service and how it differs from what is currently available.
2. List your short-, medium-, and long-term goals. What steps do you need to take to achieve each of these goals? Do you foresee any obstacles in attaining them? If so, describe them and explain how you will overcome them?
3. Contact the SBA, the SBDC, or SCORE and ask for information about your type of business. Use this information to write a paragraph about the industry in which you will be competing. What are the economic, technological, or growth trends in this industry? Is the location of your business a critical factor in its success? Why or why not?
4. Begin the financial section of your business plan by writing a report that identifies the risks your business faces. Explain how you will overcome each risk. Provide examples from magazine articles about businesspeople in your field who have succeeded when faced with similar problems.
5. Present all of the information you have compiled to your teacher or representatives from your local business community. Explain why you made the choices you did. Be prepared to defend your choices.

Planning a Career in Landscape Architecture



"We got a great deal on our house. Not only was the lawn in chaos, but there was also a problem with storm water run-off. My stepdad hired a Landscape Architect to reroute the storm water to comply with municipal regulations. Now our yard looks warm, healthy, and inviting."

Who balances the environmental, regulatory, and aesthetic outdoor needs of new developments? Who figures out how to make the external part of commercial properties look more welcoming?

Landscape Architects help municipalities, businesses, and residential locations meet ecological, land use, regulatory, and aesthetic needs of outdoor areas.

EMPLOYMENT OUTLOOK

- Faster than average job growth is anticipated.
- About one-quarter of Landscape Architects are self-employed.
- New construction and an increasing need to meet environmental regulations when planning exteriors will increase demand for qualified employees.

JOB TITLES

- Landscape Consultant
- Open Space Planner
- Residential Landscape Architect
- Project Designer
- Historical Landscape Architect

NEEDED SKILLS

- A Bachelor's degree is recommended; some positions require a Master's degree.
- Most states require licensing based on the Landscape Architect Registration Examination.

- Some states require state licensing, which focuses on state-specific environmental laws.

What's it like to work in Landscape Architecture? Givon, a self-employed Landscape Architecture Consultant, has just gotten off the phone with a client. The 300-home community planned by the client requires a community park, beautified entrances, attractive boulevards, and compliance with city zoning regulations.

To develop a bid for this project, Givon needs to meet with the developer's architects, visit the site, and meet with city officials regarding legal requirements. The final bid will include a phase-by-phase completion timeline and sketches reflecting the anticipated appearance of the neighborhood.

After lunch, Givon meets with his city's urban renewal team. The city is renovating a blighted residential area. Givon's input is needed to develop an attractive landscaping plan that will optimize the use of a small amount of land set aside for landscaping.

After dinner, Givon prepares for his morning meeting with a retail developer. Givon's recommendations for the retail parking lot design include planting many trees and shrubs throughout the parking lot. This greenery not only improves the aesthetics of the parking lot, but it also helps lessen "heat buildup" that is a common problem during hot summer weather.

What about you? Would you like to help develop landscaping plans that have a long-term beautifying effect on communities and businesses?



PREPARED SPEECH

Effective speaking skills are essential to success for entrepreneurs. As an entrepreneur you will be speaking to investors, customers, and suppliers. The Prepared Speech event lets you demonstrate your communication skills in securing, arranging, organizing, and presenting information orally.

Contestants should select a topic related to business, entrepreneurship, or Business Professionals of America and develop an oral presentation of no less than five and no more than seven minutes. This event emphasizes a scholarly approach to securing information and places emphasis on content and research. Facts and working data may be secured from any source. State and federal copyright laws must be followed in the preparation of the speech.

Each contestant must do his or her own work in researching and preparing the speech. The contestant should consider the purpose of the speech, such as to inform, to educate, to motivate, or to persuade. Contestants should also keep in mind the three basic elements of an effective speech and presentation. These three basic elements include the introduction, the body, and the conclusion. Refer to the *Sharpen Your Entrepreneurial Skills* feature in Chapter 2 for more detailed information about each of these three elements. During the speech, the contestant should be enthusiastic and use proper grammar.

The speech will be given in front of a panel of judges and a time-keeper. Contestants will be given one minute to set up for their speech. A flip chart, posters, and/or props may be used during the speech.

PERFORMANCE INDICATORS EVALUATED

- Demonstrate effective communication skills.
- Demonstrate skills in developing a speech using the three basic elements.
- Utilize non-verbal gestures as needed.
- Apply speaking techniques using appropriate tempo and pitch.
- Secure facts and data from multiple sources, emphasizing research skills.

Go to the BPA web site for more detailed information.

Think Critically

1. How can good speaking skills benefit an entrepreneur?
2. Why is research important when preparing a speech?
3. Why should you follow copyright laws when preparing a speech?
4. How do the three elements of a speech contribute to its effectiveness?

www.bpa.org

Chapter 4



© Digital Vision

Identify and Meet a Market Need

4.1 Identify Your Market

4.2 Research the Market

4.3 Know Your Competition

school.cengage.com/entrepreneur/ideas

IDEAS IN ACTION

Serving Customers' Needs

Brian Hendricks was 17 years old when he started his first business. At that time, he was a student with a knack for building and fixing computers. The idea for his business came from his frustration with his slow, boring computer. So, he built his own computer and then began building computers for others.



© Freed Photography

Brian Hendricks, founder,
StartUpPc

StartUpPC's focus is providing performance systems and quality service. Brian developed a computer program called E-Builder. With it, customers complete an electronic survey that is used to determine the best computer solution for their needs. E-Builder recommends components, software, and accessories with an explanation for each selection. It also provides the price and estimated building and shipping time.

Brian observed the residents of his community spending 30 to 60 minutes taking their computers into local computer stores for repairs. They would then have to wait for days for their return along with a big repair bill. Brian decided to give customers another option. StartUpPC services computers in the homes and offices of the customers. No charge is made until the computer is repaired to the customer's satisfaction. The technicians are willing to walk customers through the repairs that they are making so the customers might be able to fix the problems themselves should they occur again. Realizing how important computers are in the everyday lives of people, StartUpPC creates reliable and fast computers and also provides reliable and fast computer service.

Brian also saw a need for quality web sites and founded VB Solutions, Inc. to address this need. VB Solutions develops and customizes web sites and message boards. It sets up advertising contracts and works with web site owners to improve their sites. The business has designed corporate ID kits, logos, and web sites for customers all over the world.

Brian learned at a young age that "working for yourself is one of the best jobs available." He has identified a set of qualities that young entrepreneurs should possess, based on "The Five P's of Entrepreneurship." These include planning, persistence, patience, people, and profit. Brian does not believe in setting huge goals that require large investments of money. His advice is to "start small and to just not give up."

What do you know?

1. What customer need did Brian identify when he started StartUpPC?
2. Why would StartUpPC be willing to show customers how to make their own repairs?
3. What do you think about Brian's idea of starting small and not giving up?

4.1

Identify Your Market

Goals

- Identify a target market by analyzing the needs of customers.
- Explain how market segmentation can help an entrepreneur analyze a target market.

Terms

- target market
- market segments
- customer profile
- demographics
- psychographics
- use-based data
- geographic data

Focus on Small Business

Who is your customer?

Roseanne and John had their own restaurant in Los Angeles, California, when their daughter was born. Deciding that they wanted a different lifestyle for their family, they began to think about relocating and starting a new restaurant in a small-town setting. They talked about the kind of restaurant they wanted to open and what type of customer they thought would eat at their restaurant. They decided that they would target middle- to upper-middle-class families who had a love for good food, were willing to drive up to 30 miles to get it, and were willing to pay \$10 to \$15 per meal.

Work as a Team Roseanne and John put a great amount of thought into the type of customer they wanted to attract before they began to look for a location. Do you think this was a good idea or a waste of time?



© Getty Images/PhotoDisc

Think about the type of customer you want to attract.

Target Market

Entrepreneurs with exciting new ideas are sometimes so focused on their products or services that they forget about the customer. Coming up with a good idea for a business is not enough to guarantee success. Customers are the people or organizations who buy the products and services companies offer. Before establishing your new enterprise, you will have to determine who your primary customers are and whether these customers will be willing to buy your product or service. Market research is the key to finding out this information. The customer is your most important asset.

As an entrepreneur, you will need to estimate demand for your products or services by identifying your target customers. The **target market** includes the individuals or companies that are interested in a particular product or service and are willing and able to pay for it. Identifying your target market helps you reach the people who desire

your products and services. Target customers are the customers you would most like to attract. A car dealer selling moderately priced minivans would target middle-class families with children. A car dealer that offers expensive sports cars might target single people with higher incomes. If you concentrate your selling efforts on a certain type of individual, you will be likely to give those individuals exactly what they want.

Identify Your Target Market

To identify the target market for your product or service, you will need to answer the following questions:

1. Who are my customers: individuals or companies?
2. If my customers are individuals, how old are they? How much money do they earn? Where do they live? How do they spend their time and money?
3. If my customers are companies, what industries are they in? Where are those industries located?
4. What needs or wants will my product or service satisfy?
5. How many potential customers live in the area in which I want to operate?
6. Where do these potential customers currently buy the products or services I want to sell them?
7. What price are they willing to pay for my products or services?
8. What can I do for my customers that other companies are not already doing for them?

As an entrepreneur, you should put yourself in your customers' shoes before you start your business. Afterwards, you should think about your customers' needs and viewpoints everyday. By continually evaluating your market, you will be ready to respond to changes in communities, consumer tastes and buying habits, and competitors' offerings.



Why do you think it is important for a clothing store to identify its target customers?

Develop Your Reading Skills

As you read this chapter, develop questions for each section that you can use as a study guide for the chapter.

Checkpoint

What questions should you ask when identifying your target market?

Market Segments

Groups of customers within a large market who share common characteristics are known as **market segments**. Market research can be used by a business to identify market segments. Segmenting, or dividing your target market into several small groups, can help you develop a product or service that will meet specific customer needs and wants.

The process of market segmentation is important because most products and services appeal only to a small portion of the population. The leisure services market is a large market that includes many segments, such as outdoor adventurers, people who vacation frequently, couples who eat at restaurants, and more. Targeting the entire leisure market would not make sense. You would never be able to meet the needs of the entire market. Even the restaurant segment of the leisure

WHAT WENT WRONG

Price War

U-Corp was the first company in the computer industry to offer removable hard disk drives for personal computers. For years, U-Corp had a unique position in the industry and had little direct competition. Eventually, the company was making \$300 million in annual revenue.

U-Corp's first competition came from A-Corp, which offered a product similar in price and performance. A-Corp spent heavily on advertising and ran frequent reduced-price promotions. As a result, A-Corp took a large amount of business from U-Corp. U-Corp decided to try to take back the market it had lost to A-Corp and launched a multimillion-dollar marketing campaign aimed at its target market.

The two companies went head to head, selling disk drives at lower and lower prices. However, consumers do not generally need to buy multiple hard drives because of their large storage capacity. Only one company could win, and it was A-Corp. In less than two years, U-Corp suffered losses, and A-Corp bought it out.

Think Critically

1. What was U-Corp's major disadvantage in competing with A-Corp?
2. What did each company fail to realize about its customers?
3. How might the price war for removable hard drives have been avoided?



U-Corp should have considered other strategies before engaging in a price war.

services market has subsegments. Some people eat fast food on a regular basis, while others like a sit-down meal at a nice restaurant. There are people who like Italian food and others who prefer seafood or Chinese food.

Businesses can make decisions based on the information gathered on market segments. However, if the data are not analyzed correctly, the product may not meet the needs of the customers or the business might ignore a segment of the market that would be very interested in the product.

Customer Profile

A market segment is made up of people with common characteristics. The more you learn about them, the better strategy you can develop for reaching them. A very useful part of analyzing your data is the creation of a customer profile. A **customer profile** is a description of the characteristics of the person or company that is likely to purchase a product or service. A customer profile can help you understand what you need to do to meet customer demand. Customers may be profiled based on many types of data, including demographics, psychographics, use-based data, and geographic data.

SAMPLE CUSTOMER PROFILE FOR A SPORTING GOODS STORE

- Individual 23 to 52 years of age
- Participates in sports
- Wants good-quality sports equipment
- Looks for good prices
- Lives in city of Blanchester
- Average household income: \$42,000 per year

DEMOGRAPHICS Data that describe a group of people in terms of their age, marital status, family size, ethnicity, gender, profession, education, and income are called **demographics**. Women business owners between the ages of 25–40 who earn at least \$50,000 per year is an example of a market segment based on demographic data.

PSYCHOGRAPHICS Data that describe a group of people in terms of their tastes, opinions, personality traits, and lifestyle habits are called **psychographics**. People who prefer to live in a downtown setting and whose musical preference is jazz is an example of a market segment based on psychographic data.

USE-BASED DATA Data that helps you determine how often potential customers use a particular service is called **use-based data**. If you were starting a travel agency, you would want to know how often your potential customers travel.

GEOGRAPHIC DATA Data that helps you determine where your potential customers live and how far they will travel to do business with you is called **geographic data**. If you were thinking of opening a coffee shop, it would be important for you to know that people are not willing to drive more than one mile for coffee.

Once you have analyzed your target market, you will be able to develop a marketing strategy. A marketing strategy identifies those customers that you can better serve than your competitors. It can help you determine the size of your market and how many



people would be willing and able to purchase your product or service. You can design your products and services, set prices, and direct promotional efforts toward those customers.

Checkpoint

Name four types of customer data that may be analyzed in developing a customer profile.

4.1 Assessment

THINK ABOUT IT

1. Why is it so important to identify your target market?
2. How are market segments useful to an entrepreneur?
3. You are thinking about offering golf lessons in your town. What types of data would you collect to create a customer profile?

MAKE ACADEMIC CONNECTIONS

4. **MATH** Marcel wants to open a car wash after graduating from high school. For several days, he observed the cars being washed at a local car wash and recorded the information below.

Day 1	Day 2	Day 3	Day 4	Day 5	Day 6
50 cars	45 cars	48 cars	26 cars	47 cars	55 cars

What is the average number of cars washed each day? If the car wash were open only five days a week, how many cars might be washed per year?

5. **GEOGRAPHY** Think of a business you would like to open. Obtain a map of the area where you would like to locate the business. Mark the areas on the map that represent the farthest distance you believe customers would be willing to travel to do business with you. Draw a circle that encompasses the points where your customers live.
6. **COMMUNICATION** Interview a business owner. Ask the owner the eight questions listed in the chapter for identifying a business's target market. Write a report based on what you find out about the owner's target market.



TEAMWORK

Working with team members, look through magazines and newspapers for an advertisement of a new product. Based on the type of publication and the material contained in the advertisement, answer the eight questions found on page 93 about identifying a target market. Can you determine who the target market is for the product?

4.2

Research the Market

Goals

- Explain the role of market research.
- Identify the six steps involved in market research.

Terms

- market research
- primary data
- survey
- focus group
- secondary data

Focus on Small Business

Get to know your market

Roseanne and John decided that they would like to locate their business in South Carolina close to the areas where they grew up. They knew that it would be important for them to research the market in that area to be sure there was a market for the type of restaurant they wanted to open. They decided to interview groups of potential customers to gather their thoughts and opinions. They also developed a questionnaire and hired some local high school students to call residents in the community to collect more data.

Work as a Team Do you think that Roseanne and John are using good methods to gather data? Can you suggest any other ways they could find out what their potential customers thought about the business idea?



© Getty Images/PhotoDisc

Interviews are just one way to gather market research.

Role of Market Research

For your business to succeed, you need to find out who your customers are, what they want or need, and how much they are willing to pay for your product or service. To collect this information about your customers, you will perform market research. **Market research** is a system for collecting, recording, and analyzing information about customers, competitors, goods, and services. Based on the findings of market research, a business will be able to determine which marketing strategies will be most effective and most profitable. Market research has its limits because it can be very expensive and time-consuming, but it is definitely worth doing when major decisions are being made. You will draw on primary data and secondary data as you gather your information. Both types of research will help you identify ways in which you can meet customer needs.

Primary Data

Most market researchers collect primary data. Information collected for the very first time to fit a specific purpose is **primary data**. A researcher collects primary data to help identify and understand the target market. There are a few different ways to collect primary data.

SURVEY The most common type of primary market research is a questionnaire, or survey. A **survey** is a list of questions to ask your customers to find out demographic and psychographic information. A survey can be conducted by mail, over the phone, on the Internet, or in person.

OBSERVATION Market research can also involve observation. If you are considering opening a juice bar in a shopping mall, you might want to see how many customers you could attract. You could go to the mall and count the number of people purchasing drinks at various food outlets. An entrepreneur interested in starting a motorcycle repair shop might count the number of motorcycles at a busy intersection.

Famous Entrepreneur

Thomas A. Edison

Could you do your homework at night if there was no light? Thanks to Thomas Edison, you can do your homework late at night! Thomas Edison is considered to be the greatest inventor in American history.

Edison showed entrepreneurial characteristics at an early age. At the age of 12, he talked his parents into letting him go to work selling newspapers, snacks, and candy on the local railroad. Then he started an entirely separate business selling fruits and vegetables.

When Edison was 14, the pre-Civil War debates between Lincoln and Douglas were taking place. He used his access to the associated news releases that were being teletyped into the railroad station each day and published them in his own newspaper. Focusing on newsworthy “scoops,” he quickly had over 300 commuters subscribing to his paper, *The Weekly Herald*.

Edison turned on the lights for all of us with his invention of the electric light in 1879. As a young inventor with a curiosity about everything, he learned to invent only those things that people wanted. As one of the original founders of the General Electric Company, he tried to develop products that would work under ordinary conditions, would not easily malfunction, and could be easily repaired. Known as “The Wizard of Menlo Park,” which was the home of Edison’s research laboratory, Thomas Edison truly changed the world we live in!

Think Critically

Do you think it was important for Thomas Edison to try to invent items that people wanted? Do you think all inventors can become successful entrepreneurs?



© Brady-Handy Photograph Collection (Library of Congress)

How do entrepreneurs change the way we live?

FOCUS GROUPS Another way in which you could find out about the market is by conducting interviews with small numbers of people. A **focus group** is an in-depth interview with a group of target customers who provide valuable ideas on products or services. You can ask the same kinds of questions in a focus group that you would ask in a survey, but the group setting allows for more discussion and interaction regarding each question. Focus groups usually are led by a moderator, who asks questions about buying habits, likes and dislikes, and interest in particular products and services. The focus group session is recorded so that the comments can be reviewed carefully after the session is over.

DISADVANTAGES OF PRIMARY DATA While primary data can provide the most up-to-date and useful information, collecting it can be time-consuming and more expensive to gather than secondary data. As an entrepreneur, you will need to determine how much primary and secondary market research data you need to collect.

Secondary Data

Entrepreneurs also research their target markets by using secondary data. **Secondary data** are found in already-published sources. Data on population, family size, household income, economic trends, industry forecasts, and other information can be found in secondary data resources. Places to find secondary data include the following:

1. Publications issued by government and community organizations, such as the U.S. Census Bureau, the Small Business Administration, and the Chamber of Commerce
2. Books about specific industries
3. Information on web sites for government and businesses
4. Books about other entrepreneurs who set up similar businesses
5. Trade magazines and journals
6. Newspaper articles and statistics

Kisha Nichols wanted to expand her family-owned chain of retail shoe stores. She decided to perform some secondary data research and visited the local Chamber of Commerce web site. The site provided her with demographics on population for her city and county and industry forecasts for communities in her area. This information allowed Kisha to identify the largest markets as well as the markets expected to grow the most over the next 10 years. She also found information in a book on the average income of retail shoe store owners in her state. Newspaper articles gave Kisha psychographic data on people's lifestyles in her area. Most worked in professional office settings, which meant they had a need for comfortable dress shoes. Studying secondary data gave Kisha a good idea of which community might provide the best prospects for a new shoe store.

did you KNOW?

Many retail stores collect primary data through the use of scanners. The salesperson scans the universal product code (UPC) on each item purchased. The storeowner can then determine the best- and worst-selling items and adjust inventory accordingly.

Checkpoint

What types of data do entrepreneurs collect through market research?



Six Steps of Market Research

Collecting primary data can be time-consuming and expensive, but it is extremely valuable. It will tell you exactly what you want to know and uncover information you may not find through secondary sources. Conducting primary market research involves six steps as shown at the left.

1. Define the Question

In the first step in the market research process, you need to define exactly what it is that you need to know. Entrepreneurs have many concerns and questions about the businesses they are planning. By determining what they need to know, they are defining the question that will be the focus of their research.

Maggie Blandin is thinking about starting a dog-walking service. Before she invests in her business, Maggie needs to determine who would be most likely to use her service (her target customers).

2. Determine the Data Needed

Once you have defined the market research question, you are ready to determine what data you need to collect to provide the answer to your question. Entrepreneurs need to be sure that the data they collect will be helpful.

It would not be helpful for Maggie to know how many families live in the area where she wants to have her dog-walking service. She needs to know how many people living in the area are dog owners who lack the time to walk their dogs.

3. Collect the Data

Before you begin collecting data, you need to decide how you will go about gathering the data. Should you use a survey? Should you use an observation method? Is a focus group appropriate? The method you use will depend on what type of information you want to gather. For example, you can find out people's opinions in a survey or focus group, but not by observation. You should perform some secondary market research first to familiarize yourself with your market. Demographic and psychographic data, as well as information on economic trends and industry forecasts, will help you determine what kind of primary data research to perform. You can then choose the best research method for the information you want to gather.

If you choose a survey, think carefully about how long it should be, what questions it should include, how it should be administered, and how many people you should survey. If you use observation to do your research, you need to determine where and when to get the best information. If a focus group is needed, you should think about what kinds of individuals to include and what questions to ask them.

Maggie decides that a survey is the best way for her to find answers about customer preferences for a dog-walking service. Through her secondary data research, Maggie learned that 60 percent of the households in her area owned one or more dogs and that average annual household income was \$75,000. Most households had one or more adults working in a professional field. She also found that dog ownership was on the rise in her area. Based on this information, Maggie put together the survey shown on the next page. The survey asks specific questions about the lifestyles, opinions, and choices of dog owners.

DESIGN A SURVEY Making a good questionnaire is very important. Questionnaires should be kept to a page in length when read over the phone or mailed to respondents. Longer questionnaires can be used if an interview is face to face. Questions should be clear and easy to answer, and only the most important questions should be asked. If the response to a question serves no specific purpose, the question should not be used.

4. Analyze the Data

Once you have collected all your primary and secondary data, you will need to analyze and interpret the information thoroughly. The analysis should be in a written format so you can refer to it later.

Through the secondary data she obtained, Maggie found that 2,500 dogs live in her area. From her primary data research, she found that 30 percent of dog owners in her area would pay \$20 to have their dogs walked for 30 minutes. Many would pay to have them walked two or three times a week. Maggie determines that she could easily have 750 dogs to walk each week.

5. Take Action

Once you have analyzed and interpreted your data, you will need to determine how to use the data to make a decision. This is when you will develop a plan of action based on the information you found in your market research.

Maggie Blandin's market research has helped her conclude that her idea for a dog-walking service is profitable. From her market research, she has created a target customer profile of people aged 31 to 50, who travel often, work long hours, and earn \$50,000 to \$100,000 a year. She also knows the amount of money her target customers are willing to pay for her service and how much income she can expect to make.

NETBookmark

Groups of customers within a large market who share common characteristics are known as market segments. Access school.cengage.com/entrepreneur/ideas and click on the link for Chapter 4. The *You Are Where You Live* feature describes every U.S. neighborhood in terms of a wide variety of lifestyle types. Choose the PRIZM NE system and enter your own ZIP code. What results did you find? In which lifestyle type (if any) do you think you and your family fit? Now choose the ConneXions system and enter your ZIP code. Do the results differ from those found under the PRIZM NE system? Explain. Which system do you think more accurately describes your neighborhood?

school.cengage.com/entrepreneur/ideas



MARKET RESEARCH SURVEY

Thank you for participating in this market research survey. We appreciate your assistance in helping us identify the needs of pet owners in our community.

PLEASE CHECK THE BOX THAT BEST DESCRIBES YOUR SITUATION.

Age: UNDER 18 ☐ 19–30 ☐ 31–40 ☐ 41–50 ☐ 51–65 ☐ OVER 65 ☐

Gender: MALE ☐ FEMALE ☐

Number of pets: 0 ☐ 1 ☐ 2 ☐ 3 ☐ 4 OR MORE ☐

Kinds of pets: DOG ☐ CAT ☐ FISH ☐ BIRD ☐ OTHER ☐ (PLEASE SPECIFY)

IF YOU OWN A DOG, PLEASE ANSWER ALL OF THE FOLLOWING QUESTIONS.

How often do you walk your dog?

EVERY DAY ☐ A FEW TIMES A WEEK ☐ ONLY ON THE WEEKENDS ☐ NEVER ☐

Would you be willing to pay someone you trusted to take your dog for walks?

YES ☐ POSSIBLY ☐ NO ☐

If you would be willing to pay someone to walk your dog, how many times a week would you utilize this service?

EVERY DAY ☐ 2–3 TIMES A WEEK ☐ ONLY ON THE WEEKENDS ☐

How much would you be willing to pay to have your dog(s) walked for 30 minutes?

\$10 ☐ \$15 ☐ \$20 ☐ \$25 ☐ I WOULD NOT PAY TO HAVE MY DOG WALKED ☐

How often do you travel out of town?

ONCE A YEAR ☐ 2–3 TIMES A YEAR ☐ SEVERAL TIMES A YEAR ☐ NEVER ☐

Who takes care of your dog when you are out of town?

KENNEL ☐ FRIEND ☐ NEIGHBOR ☐ OTHER ☐

Would you be interested in having someone you trust take care of your pets while you are away?

YES ☐ POSSIBLY ☐ NO ☐



In her first effort to get customers, Maggie plans to create a flyer aimed at her target market, which she will distribute in neighborhoods and veterinarian offices. She also plans to distribute the flyer downtown and in other business areas where many of her target customers work.

6. Evaluate the Results

Evaluation is the last step in the market research process. It is not enough just to develop a plan of action. Entrepreneurs must regularly evaluate the actions they take as a result of the plan.

Maggie will need to evaluate the effectiveness of her flyer. If she is getting a good response from her target market, she can assume that her plan of action is effective. However, if she is not getting a good response, then she will need to revise her plan of action.

Checkpoint

What are the six steps of market research?

4.2 Assessment

THINK ABOUT IT

1. Why do entrepreneurs need to conduct market research?
2. What are the limitations of market research?
3. What is the difference between primary and secondary data?
4. Why do you think short questionnaires are more effective than long ones?
5. Why is it important to define the question you want your market research to answer?

MAKE ACADEMIC CONNECTIONS

6. **MANAGEMENT** Your family-owned business processes and sells orange juice to food distributors. In order to grow, the business needs to expand its product line. Apply the six market research steps to help determine an additional product for your business.
7. **COMMUNICATION** It is important to evaluate the effectiveness of a survey. Using the Activity CD, open the activity "Market Research Evaluation." Print a copy and complete the activity.



TEAMWORK

Working with team members, come up with a new product that you think will be very useful for students in your school. Develop a questionnaire for potential consumers of this product to gauge their interest. Have students from your school complete the questionnaire. Tabulate the results and determine if the product is a good idea.



4.3

Know Your Competition

Goals

- Explain the importance of understanding your competition.
- Determine types of competition.
- Prepare a competitive analysis.
- Describe strategies for maintaining customer loyalty.

Terms

- direct competition
- indirect competition
- competitive analysis

Focus on Small Business

Who is your Competition?

Roseanne and John needed to find out who their competition would be. They drove 30 minutes in all directions from the location they chose for their restaurant and made a list of all the restaurants they saw on their trips. They also obtained menus of the restaurants to see what type of food they offered. They even ate at several of the restaurants and observed the restaurants' strengths and weaknesses. Roseanne and John determined that their restaurant would offer a different type of food than any of their competition and that the customers in their target market would be willing to try a new restaurant.

Work as a Team How can Roseanne and John differentiate their restaurant from competing restaurants? How can they keep customers coming back?



© Getty Images/PhotoDisc

It is beneficial to check out the competition in person.

Impact of Competition

The U.S. economic system is based on private property, freedom of choice, profit, and competition. Because consumers are free to buy whatever they want from whomever they want, companies compete for their business. Most new businesses face *competitors*—companies offering similar or identical products and services to the same group of target customers. As the owner of a new business, you will have to persuade customers to buy from you instead of your competitors. You must always watch the competition and be sure that you are offering products that are of equal or better quality at the same or lower prices.

When personal computers first came on the market, Apple computers were the biggest sellers. Then IBM developed a personal computer, and soon there were many other manufacturers of personal computers. Today, customers have many choices for personal computers. All of the computer manufacturers work hard to convince customers to buy their product.

Understand the Competition

Knowing about your competition will also help you define your target market. Businesses typically enter into areas where there is competition. To survive, they have to identify some special customer need or want that is not being met. Customers may be happy with the products or services being offered, but they may be unhappy with the prices being charged. Customers might be dissatisfied with the quality of a product or service and would be willing to pay more for better quality. In either case, a customer need is going unmet by a competitor, indicating a possible opportunity for an entrepreneur.

Checkpoint

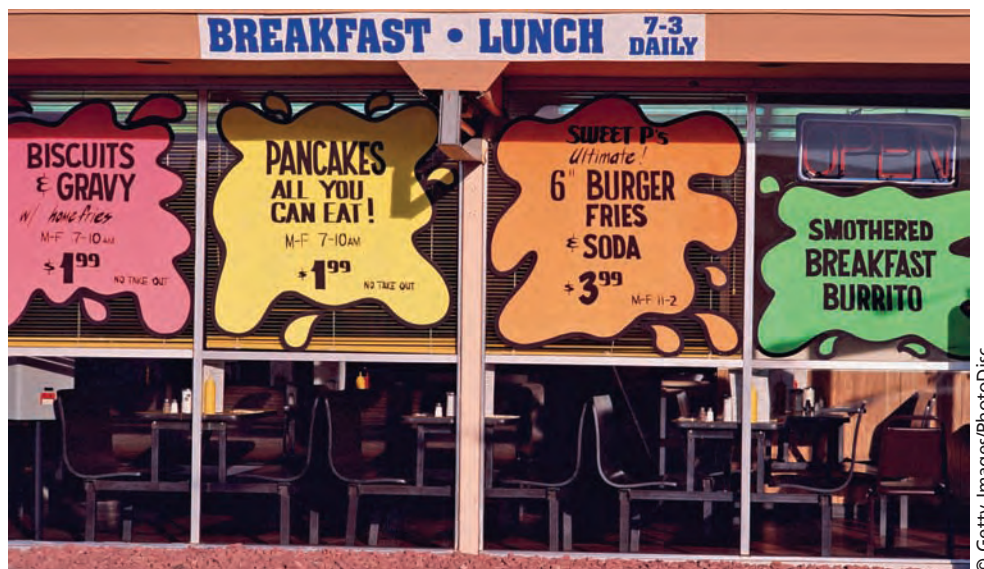
Why is it important for you to understand the competition your business faces?

Types of Competition

Competitors may be categorized as either direct or indirect competition. You will need to find ways to identify and differentiate yourself from both types of competition.

Direct Competition

Direct competition comes from a business that makes most of its money selling the same or similar products or services to the same



How could a small diner differentiate itself from larger restaurant chains?

market as other businesses. Secondary data resources can give you information on your direct competition. Your direct competitors may be in the same geographic area as your business. The telephone directory or an Internet search will help you find the number and locations of competing businesses. Your local Chamber of Commerce will also have information on competitors in your business field. Observation methods can help you learn more about your direct competitors. If you start a retail business, you can visit all of the malls, shopping centers, and retail outlets in your area.

For some businesses, direct competitors may be located far away. Carmen Quinterro publishes a travel newsletter about Ireland. Carmen's target customers live all over the United States. Her competitors include five other newsletters about Ireland as well as several travel web sites. Although Carmen's competitors are located far from her home in Chicago, they compete with her for the same target customers.

Indirect Competition

Indirect competition comes from a business that makes only a small amount of money selling the same or similar products and services to the same market as other businesses. Locating your indirect competition is more difficult than finding direct competitors. You should first think of all of the possible businesses that can compete with you indirectly. A large department store may stock some of the most popular products carried by a privately owned specialty shop. The department store offers many other lines of merchandise as well. It makes only a small amount of money on the same items that the specialty shop offers. This makes the department store an indirect competitor to the specialty shop.



What kind of indirect competition might a small florist face?

Large Retailers

When a large retailer enters a community, it can be a source of direct and indirect competition for many other businesses. Large retailers like Wal-Mart bring lower prices and jobs to a community, but many small businesses find it hard to compete with them. Some of the smaller, locally owned retailers often are forced out of business. Some of the reasons that it is difficult for entrepreneurs to compete with large retailers include the following:

1. **Large retailers usually are able to keep larger quantities of products in stock.** They can purchase inventory in bigger quantities because they have more revenue and larger storage areas. Bigger orders result in volume discounts, and the savings can be passed to consumers in the form of lower prices.
2. **Large retail chains do not rely on a single product line.** If one product line does poorly, a large retail store does not go out of business because it has other successful product lines. Small businesses have risks associated with having only one product line. If its product falls out of favor with consumers, it has no other product lines to make up the difference.
3. **Large companies usually have more resources to devote to advertising.** A larger company makes more revenue and can hire advertising professionals to create effective advertising to attract more customers.

Checkpoint

What is the difference between direct and indirect competition?

Competitive Analysis

Identifying and examining the characteristics of a competing firm is called a **competitive analysis**. Analyzing the strengths and weaknesses of your competition will help you figure out what you can do to get customers to buy from your business. Follow these steps to begin your competitive analysis:

1. **Make a list of your competitors.** Using the Internet and *The Yellow Pages* and driving through the area in which you plan to locate your business are good ways to identify your competition. You can also talk to potential customers to find out with whom they are currently doing business. Review trade magazines and newspapers to see who is advertising the product or service you plan to offer.

BE YOUR OWN BOSS

You opened The Sweet Shop, a candy and ice cream store, on the grounds of a beach resort hotel. You get a steady stream of new customers as guests from the hotel visit your shop. However, you want to attract local residents from the community to your business to help grow a customer base year-round. You decide that a frequent-buyer program is one way to get customers to visit and return to your business. What type of frequent-buyer program would be good for The Sweet Shop? Design a flyer that would introduce the program to customers. Also, design a card that you would give customers to identify them as frequent buyers.

2. **Summarize the products and prices offered by your competitors.** Investigate the products or services your competition offers for sale. How are they different from yours? Examine the price ranges of your competitors and determine how they compare to what you plan to charge. Are your prices higher or lower?
3. **List each competitor's strengths and weaknesses.** What does the competitor do that no one else does, or what does it do better than everyone else? Where are your competitors located? Determine if their location is better, worse, or about the same as the planned location for your business. Compare the competitors' facilities to the planned facility for your business. Are their facilities better, worse, or about the same as yours? What attracts customers into your competitors' facilities? How will you compete with these strengths? What are some of the weaknesses of your competition? How can you use these weaknesses to your advantage?
4. **Find out the strategies and objectives of your competitors.** A copy of your competitors' annual report would have this information.
5. **Determine the strength of the market.** Is there an increase in demand for the product or service you plan to offer? Will there be enough customers for everyone in the market? What are the industry forecasts?

Interjit Singh wants to start a premier car wash in an expensive suburb of Washington, D.C. He does a competitive analysis as shown below. He researches his direct and indirect competition. He finds that Royal Hand Wash is able to charge twice the price of the other competitors even though its location is not the best. Royal Hand Wash guarantees nonscratch car washes and waxes done by people, not machines. Because Interjit's business will also offer car washes, waxes, and detailing done by hand, Royal Hand Wash is the direct competition. All other car wash businesses, including gas stations with automatic car wash machines, are his indirect competition. Royal Hand Wash's location and prices are its biggest weaknesses, so Interjit plans to choose a prime location for his car wash and charge lower prices.

Checkpoint

What is the purpose of a competitive analysis?

ANALYSIS OF COMPETITORS

Competitor	Price	Location	Facility	Strength	Weakness	Strategy
Standard Gas	\$6.00	Excellent	Good	Excellent location	Car wash not easily accessible	Target a different market
Lakeland Car Wash	\$5.50	Fair	Good	Low price	Location	Target a different market
Ray's Car Wash	\$5.00	Good	Fair	Low price	Facility	Target a different market
Royal Hand Wash	\$11.50	Fair	Excellent	Excellent facility	Location	Offer lower prices, better service, more convenient location

Maintaining Customer Loyalty

Getting customers to buy your products and services instead of competitors' is only one step in running a successful business. Once you get the customers, you must make sure they remain loyal to you and keep coming back.

Listen and Respond to Feedback

To retain customers, you will need to continually ask customers for their opinions about your business and respond to their feedback. Businesses that ignore customer concerns will not stay in business long. Businesses stay in touch with their customers' needs in different ways. Some businesses may call customers after sales are made to ensure they are satisfied with their purchase. Many companies have a customer feedback box where customers can put complaints or positive comments about the business. You can also design a survey for your customers to complete.

Jason Rose's business, the Metropolitan Athletic Club, closed because of his failure to respond to customer feedback. Club members had repeatedly complained about the lack of cleanliness in the locker rooms and the lack of available weight machines during peak hours. Jason ignored his customers' complaints, believing that the excellent location and low monthly fee would ensure his success. Jason learned from his mistake.

When he opened his next athletic club, he immediately tried to find out what customers wanted by conducting a market research study. His study revealed, among other things, that he should offer more aerobics classes and put high-speed hair dryers in the locker rooms. Due to his focus on customer satisfaction, Jason's club is doing very well and attracting new members all the time.



© Getty Images/PhotoDisc

How could a fitness club maintain loyalty among its clients?

Other Strategies for Maintaining Loyalty

To maintain customer loyalty, businesses use many strategies. The main purpose of these strategies is to keep customers happy so they will return to the business. Some of the most basic customer loyalty strategies businesses use include the following:

- Superior service
- More convenient hours than other businesses



- Easy return policies
- Store-specific credit cards
- Personal notes or cards for birthdays or as a way to say thanks for the business
- Frequent-buyer programs

Kathleen McGuire, the owner of Flower Markets, encourages shoppers to buy all of their flowers from her garden store by issuing them a frequent-buyer card, which she stamps every time a purchase of \$10 or more is made. Once the card has been stamped 10 times, customers can redeem the card for a free bouquet of flowers.

Checkpoint

What are some strategies for maintaining customer loyalty?

4.3 Assessment

THINK ABOUT IT

1. Why should entrepreneurs analyze both direct and indirect competitors?
2. Why is a competitive analysis important to an entrepreneur?
3. Why can customer feedback be considered a type of market research? Is this market research more or less valuable than other research you conduct? Explain your answer.

MAKE ACADEMIC CONNECTIONS

4. **MANAGEMENT** Devise a plan to maintain customer loyalty for a hair salon. Create an advertisement to let your customers know about this plan.
5. **COMMUNICATION** Shontel Washington just opened an art gallery. He would like feedback from the people who visit the gallery. Develop a short questionnaire that would help Shontel learn more about his customers' feelings toward his business.
6. **TECHNOLOGY** Using the car wash data shown on page 108, enter the prices into a spreadsheet. Use the spreadsheet to create a bar graph that will help Interjit Singh analyze the data.



TEAMWORK



Working with team members, choose a successful business in your area. Then choose three competing businesses. Using the Activity CD, open the activity "Competitive Analysis." Print a copy and complete the activity by analyzing each business using the five steps listed in this lesson.



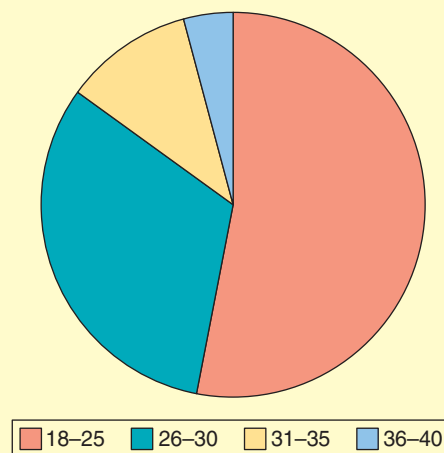
Sharpen Your Entrepreneurial Skills

Using Spreadsheets to Analyze Data

Spreadsheets are a powerful tool for analyzing, sharing, and managing numerical data. Entrepreneurs can use spreadsheets to analyze market research, prepare budgets, measure performance, and create financial statements. One of the most valuable uses of spreadsheets is creating charts and graphs. Charts and graphs can improve decision making by presenting data in an easy-to-read, understandable format. Line graphs, bar charts, and pie charts are among the most commonly used visual aids.

Spreadsheets are especially useful in analyzing market research results. Gena has decided that she wants to open a coffee shop in her community. She wants to determine the age of her target market. She surveys 25 people in each of the following age groups: 18–25; 26–30; 31–35; and 36–40. She enters her survey results into a spreadsheet and creates the following pie chart. The pie chart clearly shows that consumers between the ages of 18–25 are more likely to buy coffee on their way to work.

Consumers Who Buy Coffee on Way to Work



TRY IT OUT

Maggie Blandin conducted research for her dog-walking business by surveying 2,500 dog owners. She asked what price owners would be willing to pay for a dog-walking service. She collected the following data:

Number of People	Price
500	\$10
250	\$15
750	\$20
500	\$25
500	\$ 0 (not interested)

Enter this data into a spreadsheet and create a pie chart to help Maggie determine the price she should charge for her dog-walking service. Experiment with the different kinds of charts and graphs you can create.

Chapter 4 | Assessment

SUMMARY

4.1 Identify Your Market

1. Before starting a new business, you must determine who your primary customers are and whether they will be willing to buy your product or service. Understanding your customers and their needs and wants is one of the most important aspects of running a business. Market research is key to finding out this information.
2. You should develop a customer profile and decide which segment(s) of the market to target. Markets may be segmented based on many factors, including demographics, psychographics, use-based data, and geographic data.

4.2 Research the Market

3. Market research is important because it helps you find out what your customers need and want. It also helps you understand your competition. Primary data are collected for the very first time to fit a specific purpose. Primary data may be collected from surveys, focus groups, and observation. Secondary data are found in already-published sources.
4. The six steps of market research are: (1) define the question, (2) determine the data needed, (3) collect the data, (4) analyze the data, (5) take action, and (6) evaluate results.

4.3 Know Your Competition

5. Entrepreneurs must understand their competition to help identify any currently unmet customer needs and wants.
6. All businesses have both direct and indirect competition. Direct competition comes from a business that makes most of its money selling the same or similar products and services to the same market. Indirect competition comes from a business that makes only a small amount of money selling the same or similar products to the same market.
7. Creating a competitive analysis involves the following steps: (1) make a list of competitors, (2) summarize products and prices offered by competitors, (3) list each competitor's strengths and weaknesses, (4) find out strategies and objectives of competitors, and (5) determine the strength of the market.
8. There are many ways to maintain customer loyalty. You should ask for and respond to customer feedback. Offering frequent-buyer discounts and superior service also promote customer loyalty.

What do you know now?

Read Ideas in Action on page 91 again. Then answer the questions a second time. How have your responses changed?

VOCABULARY BUILDER

Match each statement with the term that best defines it. Some terms may not be used.

1. A description of the characteristics of the person or company that is likely to purchase a product or service
2. Data that describe a group of people in terms of their age, marital status, family size, ethnicity, gender, profession, education, and income
3. An in-depth interview with a group of target customers who provide valuable ideas on products or services
4. Information collected for the first time to fit a specific purpose
5. A system for collecting, recording, and analyzing information about customers, competitors, goods, and services
6. Data that describe a group of people in terms of their tastes, opinions, personality traits, and lifestyle habits
7. Data found in already published sources
8. A business that makes most of its money selling the same or similar products or services to the same market as other businesses

- a. competitive analysis
- b. customer profile
- c. demographics
- d. direct competition
- e. focus group
- f. geographic data
- g. indirect competition
- h. market research
- i. market segments
- j. primary data
- k. psychographics
- l. secondary data
- m. survey
- n. target market
- o. use-based data

REVIEW YOUR KNOWLEDGE

9. Which of the following is *not* a reason that entrepreneurs need to know who their customers are?
 - a. customers are a business's most important asset
 - b. companies cannot remain in business without customers
 - c. customers have no influence on product or services offered
 - d. knowing who your customers are can help you estimate demand for products and services
10. To identify your target market, you need to know
 - a. who your customers are
 - b. how old your customers are
 - c. where your potential customers currently shop
 - d. all of the above
11. Data that helps you determine where your potential customers live and how far they will travel to do business with you are
 - a. demographics
 - b. psychographics
 - c. use-based data
 - d. geographic data
12. Which of the following is *not* an example of primary research?
 - a. conducting a survey
 - b. obtaining statistics from a government web site
 - c. observing customer behavior
 - d. all of the above are examples of primary data research
13. Sources of secondary data include all of the following *except*
 - a. customer feedback from a survey
 - b. publications issued by government and community organizations
 - c. trade magazines and web sites
 - d. newspaper articles

14. **True or False?** Two disadvantages of collecting primary data are the costs and time involved.
15. It is difficult for small businesses to compete with large retailers because
 - a. large retailers are able to order and stock products in larger quantities
 - b. large retail chains don't rely on a single product line
 - c. large companies have more resources to devote to advertising
 - d. all of the above
16. Which of the following is *not* a step involved when preparing a competitive analysis?
 - a. list all competing businesses in your immediate area
 - b. create a customer profile
 - c. list your competitors' strengths and weaknesses
 - d. summarize products and services offered by competitors
17. **True or False?** Businesses do not need to identify their target market in order to succeed.
18. Which of the following is *not* a good way to get customer feedback?
 - a. check with your competition
 - b. call customers the day after they make a purchase
 - c. use a customer feedback box
 - d. have customers complete a survey after shopping with you
19. Which of the following is a strategy for maintaining customer loyalty?
 - a. keeping standard business hours
 - b. adhering to strict return policies
 - c. offering superior service
 - d. none of the above
20. **True or False?** Longer questionnaires are always better because you can collect more information.

APPLY WHAT YOU LEARNED

21. Set up an interview with a local entrepreneur to find out how he or she identified the target market, what kind of market research was conducted, what kind of competition the business faces, and how customer loyalty is maintained. Before conducting the interview, compile a list of questions to ask the owner. Present your findings to the class.
22. You want to start a computer service company that keys and prints professional-looking term papers and resumes for students in your school. Design a survey that would help you determine if there is a market for your company. Determine the best way to administer the survey.

MAKE ACADEMIC CONNECTIONS

23. **MATH** You have collected primary data that indicates three-quarters of the people in your town would switch dry cleaners if they could save 50 percent on their dry cleaning. If the average resident in your town spends \$7 a week on dry cleaning and the

town has 5,000 residents, how much revenue could you expect to earn per year by opening a discount dry cleaner?

24. **MANAGEMENT** Maggie Blandin, who wants to open a dog-walking business in your town or city, has asked for your help in collecting data. Call your local Chamber of Commerce to gather demographics and psychographics for your community. Also ask for statistics on dog ownership in your area.
25. **RESEARCH** Use the Internet to find the names of four companies that might be able to help you conduct market research. Record information such as how long the company has been in business and what kinds of market research the business does. Write your findings and compare them with the findings of other students.

WHAT WOULD YOU DO?

You are having a luncheon meeting with one of your suppliers at a local restaurant. You see the owner of a business that is your main competitor across the restaurant having lunch with someone you do not recognize. They finish eating, pay their check, and leave while you are still at your table. After they leave, you notice that a notebook was left in one of the chairs at their table. You go to the table and pick up the notebook and see that it is their marketing strategy for the upcoming year. What would you do? Would you consider it your lucky day and read their strategy or would you turn it in to someone at the restaurant? Why did you choose the action you did?

BUILD YOUR Business Plan *Project*

This activity will help you develop the business plan for your business idea.

1. Identify the target market for your business. Use secondary data sources to help you assess demand for your product or service.
2. Using the secondary research, develop a customer profile for your business. Which market segment of your industry are you targeting? Be specific.
3. Conduct primary research for your business, using the steps outlined in Lesson 4.2. Develop a questionnaire that will give you the information you need. Ask at least 30 people in your target market to complete the survey. Analyze your results and determine what course of action you will take.
4. Determine who your competitors are, both direct and indirect. Using the Activity CD, open the activity "Competitive Analysis." Use the chart to prepare a competitive analysis for your business. Determine a strategy for dealing with each competitor.
5. What are your strategies for maintaining customer loyalty? Describe them and give reasons why you think each will work.



Planning a Career in Marketing Research



"My little sister decided to start a babysitting service. To tailor her business to meet client needs, she asked neighbors with children to complete an online survey regarding their child care needs. The results she compiled from the free online survey helped her put together a service and fee schedule."

How do organizations determine what services to offer? How do manufacturers determine which product features are the most important to include in a product?

Marketing research helps companies and organizations decide how to best meet the needs of their clients. Marketing research surveys provide a targeted, concise method to collect and analyze marketing data.

EMPLOYMENT OUTLOOK

- Faster than average job growth is anticipated.
- Globalization, an increasingly competitive marketplace, and better educated consumers all contribute to the increased need for marketing research.
- Outsourcing will create opportunities at consulting and marketing research firms.

JOB TITLES

- Market Research Analyst
- Mobile Video Research Manager
- Questionnaire Development Manager
- Market Research Coordinator
- Marketing Communications Specialist

NEEDED SKILLS

- A Bachelor's degree is required. Advancement may require a Master's degree or a Ph.D.

- To keep up with technology changes, continuing education is necessary.
- A blend of quantitative and qualitative coursework is helpful.

What's it like to work in Marketing Research Sales at a local gift shop have been lagging, and the owner has contracted with Tess, a self-employed Electronic Marketing Survey Writer, to create a marketing research study. The store is an independent store with a limited budget, so Tess decides to use one of the free online survey services to gather data from existing customers. The store's mailing list will be used to send customers an electronic invitation to participate in the survey. As an incentive, customers will be offered a 5 percent discount on their next purchase.

During the afternoon, Tess works on preparing a summary report for a restaurant chain. The restaurant wanted to obtain feedback on the service, the environment, and the food quality while all were still fresh on customer's minds. So Tess used a survey service that collected data via cell phones. Upon receiving their restaurant bills, clients who had cell phones were instructed how to log on to a web site where they could answer a brief online survey about their dining experience. Customers were also looking forward to receiving a free dessert upon their next visit as a reward for survey participation.

What about you? Would you like to help a variety of businesses improve their understanding of customer preferences by developing marketing research surveys?



MULTIMEDIA PRESENTATION

Multimedia presentations have become a common form of marketing for businesses and organizations. Individuals who demonstrate the ability to effectively use presentation technologies and software to deliver a message are in high demand for marketing positions. Each year FBLA will select a multimedia national topic for one, two, or three students to prepare. Multimedia presentations must be two to four minutes in length, and teams will be allowed nine minutes to describe the project. Five points will be deducted for any presentations over nine minutes in length. Judges have three minutes to ask questions about multimedia presentations. Entries for this category must include two DVDs and a read me file (300 words or less) noting software used, sources of information, and instructions on running the presentations.

TOPIC Super Bowl sponsors are needed to help cover the high costs of this sporting event. Prepare a multimedia presentation that will act as a recruiting tool for corporate sponsors of the Super Bowl. Prepare a customer profile that lists the characteristics of the person likely to watch the Super Bowl. Then make a list of the companies that sell products or services that would appeal to the Super Bowl audience. Use this information to determine a target market for your presentation. Because the price for Super Bowl sponsorship is high, the presentation should emphasize the benefits to potential sponsors, such as increased exposure in large markets.

PERFORMANCE INDICATORS EVALUATED

- Develop a convincing multimedia presentation.
- Recognize and respect copyright issues.
- Develop and support a theme with a multimedia presentation.
- Make use of and implement innovative technology in a multimedia presentation.
- Set priorities and manage time to prepare and present an effective multimedia presentation.

Go to the FBLA web site for more detailed information.

Think Critically

1. Why must the Super Bowl use a multimedia presentation to attract new corporate sponsors?
2. What kind of music or visual images would be good for a Super Bowl multimedia presentation?
3. Why must the presentation emphasize the potential return on investment for corporate sponsors of the Super Bowl?
4. What is the value of being associated as a financier of the Super Bowl?

www.fbla-pbl.org

Chapter 5



Market Your Business

5.1 Develop the Marketing Plan

5.2 The Marketing Mix—Product

5.3 The Marketing Mix—Price

school.cengage.com/entrepreneur/ideas

IDEAS IN ACTION

Turning Creative Fun into Dollars

Sheri and Rich Schmelzer of Boulder, Colorado, are the founders of Jibbitz. What's a Jibbitz, you may ask? Several years ago, Sheri and Rich didn't know either. Sheri was a stay-at-home mom with three children. They always had at least 12 to 15 pairs of Crocs—a type of colorful, sandal-like footwear with ventilation holes—in a pile at their back door. One day, Sheri was having fun experimenting with decorating the Crocs by sticking decorative pieces in the holes of the shoes. She used buttons, rhinestones, and other things she had lying around the house. Showing the decorated shoes to Rich when he returned home from work, a "light bulb" went off. Using his business experience and knowledge, the business got its start.



Sheri and Rich Schmelzer, founders of Jibbitz

© AP Photo/David Zalubowski

After experimenting with several different versions, Sheri and Rich found a secure way to attach the decorations so that they would fit snugly in the holes. Looking for a domain name for a web site, they thought about using the name Fliberty-Jibbet—a nickname Rich used for Sheri. Sheri liked the word but thought it was too long for a domain name, so she shortened it and Jibbitz was born.

Once the web site was up and running, the Schmelzers were featured in a short segment on the local news. Orders began to come in like crazy. Sheri's parents came to their house every weekend to help by gluing decorations together and getting orders ready for shipment.

Once they realized how big the market for Jibbitz was, they needed to find a mass manufacturer. Along with individual orders to fill, many retailers wanted to buy their products in quantity. The Schmelzers used a home equity loan to finance their first order from a factory in China.

A year later, the Schmelzers hit it really big when Crocs, Inc., acquired their business for \$10 million. Sheri and Rich still run the company and now have 50 employees and over 4,000 retail outlets worldwide. They are very proud of the company they have built and plan to stay involved.

What do you know?

1. Why do you think Jibbitz are so popular?
2. How important do you think the decision to market Jibbitz on the Internet was to the success of the company?
3. What do you think is different for the Schmelzers since they sold Jibbitz to Crocs, Inc.?

5.1

Develop the Marketing Plan

Goals

- Explain the importance of marketing a business.
- Discuss how to develop a marketing strategy for a business.
- Describe what information is included in a marketing plan.

Terms

- marketing
- marketing concept
- marketing mix
- marketing strategy
- marketing plan

Focus on Small Business

Is a marketing plan always necessary?

Wanda loved jewelry and had spent much time studying the work of famous jewelry designers. She also had taken some beading classes at the local recreation center. She decided that she wanted to open her own jewelry design business. She conducted market research and found that there was an interest in custom-designed jewelry in the target market she defined. Now she's ready to think about how to market her business. She knows that marketing is very important and wants to be sure that she spends the money she has budgeted for marketing wisely. She contacts the SBA, and it advises her to develop a marketing plan. She is not sure that this is a wise use of her time, but she sets out to learn more about a marketing plan.

Work as a Team Because Wanda has already found that there is a market for her jewelry designs, discuss whether she would be wise to spend time developing a marketing plan. Should she just start making jewelry and see what happens? Make a recommendation to Wanda and explain your reasoning.



© Getty Images/PhotoDisc

A marketing plan lays the foundation for success.

What Is Marketing?

As defined by the American Marketing Association, “marketing is an organizational function and a set of processes for creating, communicating, and delivering value to customers and for managing customer relationships in ways that benefit the organization and its stakeholders.” To simplify this definition, **marketing** is all of the processes—planning, pricing, promoting, distributing, and selling—used to determine and satisfy the needs of customers and the company. This definition demonstrates the importance of the customer.

It is very important to conduct market research to discover what products or services customers want to buy. Using the primary and secondary data that is gathered through market research helps

entrepreneurs develop a marketing concept for the business. The **marketing concept** uses the needs of customers as the primary focus during the planning, production, distribution, and promotion of a product or service. To use the marketing concept successfully, businesses must be able to:

- Identify what will satisfy the customers' needs and wants
- Develop and market products or services that customers consider better than other choices
- Operate profitably

Marketing Mix

An important part of implementing the marketing concept is developing a marketing mix that helps meet customer needs and enables the business to earn a profit. The **marketing mix** is a blending of the product, price, distribution, and promotion used to reach a target market. For example, once you have determined what product or service meets customers' needs, you must determine the right price for it, make it available to the customers in the right places, and then let your target market know about it.



How does the marketing mix for consumer products help meet consumer needs?

© Digital Vision

Develop Your Reading Skills

As you read this chapter, make a list of the marketing strategy components and the information you will include about each one in your marketing plan.

Checkpoint

Why is marketing important to a business?

The Marketing Strategy

As a business owner, you will need to outline the goals you want to accomplish through your marketing efforts. Once you have identified your goals, you will need to develop a **marketing strategy**, which is a plan that identifies how these goals will be achieved. In your startup marketing plan, your strategy should address:

- Product introduction or innovation
- Pricing
- Distribution
- Promotion
- Projected profitability
- Sales or market share

It is important that your marketing strategy be consistent with the overall goals you have set for your business. Be sure that the strategy will actually work for you and is within the resources you have



available. Your marketing goals should be written following the SMART guidelines in Chapter 1. These goals should reflect your short-term, medium-term, and long-term plans for your business. What do you want your marketing efforts to achieve for your business? Do you want to offer additional products or services after one year? Perhaps in five years, you want to sell your product internationally. Establishing short-, medium-, and long-term marketing goals ensures that the marketing you do today fits in with the vision you have for your business tomorrow.

Short-Term Goals

Short-term goals are what you want your business to achieve in the next year. They can be stated in terms of number of customers, level of sales, level of profits, or other measures of success.

Identifying your short-term goals will help you determine how to target your marketing. If your goal is to build a customer base, you may decide to keep prices low and spend more money on promotion. If your goal is to have a positive cash flow, you may decide to price your products or services higher.

Luisa Ramirez, a 32-year-old entrepreneur, wants to open a gourmet food shop in her community. In the short-term, Luisa wants to generate traffic into her store. Because of that goal, her marketing

Famous Entrepreneur

Sergey Brin and Larry Page

What would the Internet be like if there was no Google? Just what is a Google? Thanks to Sergey Brin and Larry Page, we have Google and an explanation of the name. “Googol” is the mathematical term for a 1 followed by 100 zeros. The term was coined by the nephew of Edward Kasner, an American mathematician. Brin and Page chose a variation of this term for their company. When they started their business, Brin and Page “set out to organize the world’s information and make it universally accessible and useful!”

Brin and Page developed a new approach to online searching while they were students at Stanford University. Using that approach, they launched Google in September of 1998 as a privately held company.

Today, Google is one of the world’s best-known brands. Most people have learned about Google by word of mouth from satisfied users.

Google generates revenue by selling advertising space. Ads are displayed on search results pages that are relevant to the content on the page. Google tracks customer traffic to measure the cost-effectiveness of the online advertising.

Today, Brin and Page share a net worth of \$16.6 billion. Google handles over 2.5 billion search inquiries daily. That’s not bad for a data center that started in a dorm room!

Think Critically

Have you ever used Google? Why do you think people choose Google over other search engines?



© AP Photo/Gautam Singh

How has the Internet provided new opportunities for entrepreneurs?



© Getty Images/PhotoDisc

Why is it important to have a marketing strategy for your business?

strategy focuses on establishing a customer base. She creates a list of short-term goals based on product, price, distribution, and promotion.

Medium-Term Goals

Medium-term goals describe what you want your business to achieve in the next two to five years. Although your marketing strategy will be determined largely by your short-term goals, you will need to make sure that the strategy you are planning will make it possible for you to achieve your medium-term goals.

Luisa wants her business to become the most successful gourmet shop in her community by increasing her customer base and her total sales. She hopes to expand the offerings in her store to include more international foods as well as specialty items from local suppliers. In addition to running her store, in five years Luisa hopes to expand her business to include catering.

Long-Term Goals

Long-term goals show where your business will be 5, 10, and even 20 years from now. Thinking about what you want the business to do in the long term can help you think about how to market your business today.

Luisa eventually would like to establish a mail-order division of her business. She does not let her long-term plans for a mail-order division change her thinking about how to market her store today. Knowing what she wants in the long run, however, motivates her to work very hard to make her store a success so that she can use it as a foundation to develop a mail-order business.

Checkpoint

Why is goal setting important when developing a marketing strategy?



Write Your Marketing Plan

When your goals and marketing strategy have been determined, you will be ready to write your final marketing plan. The purpose of the **marketing plan** is to define your market, identify your customers and competitors, outline a strategy for attracting and keeping customers, and identify and anticipate change. A written marketing plan will help you determine whether it is solid and all parts are consistent. Your written plan becomes a guiding document as you operate your business. You can always review it later to determine if you need to change the way you are marketing your business. The marketing plan becomes a part of your business plan. Having a marketing plan as part of your business plan is essential when you seek financing for your business. Investors will expect your marketing plan to answer the following questions:

- What product or service will I offer?
- Who are my prospective customers?
- Is there a constant demand for this product or service?
- How many competitors are providing the same product or service?
- Can I create a demand for the product or service I want to offer?
- Can I compete effectively in price, quality, and delivery of my product or service?

To answer these questions effectively, the marketing plan for your business must include information on the following topics:

- | | |
|-----------------------|--------------------------|
| 1. Product or Service | 5. Business Location |
| 2. Target Market | 6. Pricing Strategy |
| 3. Competition | 7. Promotional Strategy |
| 4. Marketing Budget | 8. Distribution Strategy |



What kinds of information do you think should be included in a marketing plan for a small, locally owned bike shop?

As part of your marketing plan, you should include performance standards that will help you measure your effectiveness. Researching industry norms and past performances will help you develop appropriate standards. After your marketing plan has been implemented, you should compare your actual results to your performance standards. It is helpful to examine your performance quarterly. Questions to ask yourself include:

- Am I meeting sales forecasts?
- Is my promotional campaign reaching the target market?
- Is my company doing everything it can to meet customers' needs?
- Is it easy for my customers to locate my product and is it competitively priced?

Checkpoint

Why is it important to put your marketing plan in writing?

5.1 Assessment

THINK ABOUT IT

1. What is the marketing mix?
2. What is the relationship between short-term goals and medium-term goals?
3. What topics should be included in the marketing plan?

MAKE ACADEMIC CONNECTIONS

4. **MATH** Akeo Goto has opened a pet grooming business. He estimates the annual sales of the pet grooming market in his community to be about \$325,000. There are two pet grooming businesses in town already. If Akeo achieves his five-year goal of capturing 45 percent of the market, how much will he earn in his fifth year?
5. **COMMUNICATION** Think of a local business with which you are familiar. Make a list of questions you would like to ask the owner about the marketing plan for the business. Contact the business owner and make an appointment to discuss the questions. Report your findings to your classmates.



TEAMWORK

Working in a team, choose one of the following businesses: Mexican restaurant, wholesaler, health-food store, or advertising agency. Brainstorm a list of short-, medium-, and long-term goals for the business. Make a list of these goals and post them on the wall in your classroom. Discuss the goals your team set with your classmates.



5.2

The Marketing Mix—Product

Goals

- Explain how the marketing concept affects decisions regarding the product mix.
- Define and describe the importance of product features, branding, and positioning.

Terms

- product mix
- features
- branding
- positioning

Focus on Small Business

Does location affect image?

Chase has a strong interest in men's clothing. During high school and college, Chase worked at several upscale men's stores in the Seattle area. When he graduated from college with a degree in retail marketing, he decided that he wanted to open his own upscale clothing store for men. In determining the startup costs for his business, he realized that the rent for the space in an upscale mall with specialty boutiques was too expensive. In looking for space he could afford, he found a site in a medium-sized strip mall. The other stores in the mall are discount stores, but he wants to promote his business as an "upscale, specialty store."

Work as a Team Do you think the location of Chase's store will affect its image and ability to attract the target customer? What do you think Chase should do? Should he change the focus of his business for this location?



© Getty Images/PhotoDisc

Location can help you reach your target customers.

The Marketing Concept and the Product

Once you have determined what kind of business you will run, you will need to make decisions about the products that you will sell. To select your products, think carefully about which products and services most appeal to your target customers. If you can convince your customers that your products satisfy their needs better than any competitor's products, then your products become a marketing tool for your business.

The marketing concept is the belief that the wants and needs of customers are the most important consideration when developing any product or marketing effort. Over the past 50 years, consumers have become more educated, and competition has increased to include the

global market. This has led to a change in the U.S. market, from being a product-driven market to one that is consumer-driven. The marketing concept can give small businesses an advantage over larger businesses. Small businesses can get to know their customers better than larger businesses. They can be more responsive and have more flexibility when trying to satisfy customer needs.

In the newspaper in Luisa's community, there was a recipe for a pasta dish using a special type of cheese that Luisa did not carry in her gourmet food store, and she knew none of the local grocery stores stocked it. However, she knew that many of her customers liked to try out the recipes from the paper, so she immediately got on the phone with a supplier to get the cheese in stock the next day.

did you KNOW?

According to Research and Markets, a leading source for international market research and market data, U.S. companies budget over \$1 trillion annually for marketing.

Product Mix

The different products and services a business sells are its **product mix**. In a consumer-driven economy, entrepreneurs realize that sometimes they must include products in their mix as a convenience for customers even though they may not be profitable. This will give the appearance to customers that the store has everything they need. It has been found that often a small percentage of the product selection makes up the majority of the sales revenue.

Luisa's Gourmet Luxuries will sell hundreds of different packaged goods, from imported Italian olive oil and pastas to Mexican rice. Luisa will also offer a wide selection of fresh foods, including cheeses, fruits, vegetables, and baked goods. To determine her product mix, Luisa lists the various departments she plans to establish in her store. She then lists the products that each department will carry. Luisa knows that most people coming into her store are looking for gourmet foods, but she decides to carry a small selection of pasta-making machines and espresso coffee makers. Although these items will not be a large source of revenue for her, it will show customers she can meet all their needs.



© Getty Images/PhotoDisc

How does a business's product mix help to satisfy customers?

Checkpoint

How does the marketing concept affect decisions made about the product mix?

Development of Features, Branding, and Positioning

Consumers buy a product because it meets their needs. However, there is much more to a product than consumers may realize. The many aspects of a product that a business must spend time developing include its features, branding, packaging, labeling, and positioning.

Selecting Product Features

The total product includes its **features**, which are product characteristics that will satisfy customer needs. Features include such things as color, size, quality, hours, warranties, delivery, and installation. You will need to consider your target market when selecting product features.

WHAT WENT WRONG ?

Packaging Matters

Katharine had developed a new line of dog grooming shampoo. She spent a large amount of time researching what should go into the shampoo and had the product tested to be sure it met safety standards. Her next step was to choose a way to package the shampoo. She decided that instead of a bottle, she would have the shampoo packaged in individual foil packets. She boxed the packets six to a box and set the price.

Her initial sales were good, but she was not getting repeat sales. After three months, her revenue decreased. She was unable to keep up with the expenses of running her business with no incoming revenue.

She decided to survey her customers to find out why they were not ordering more shampoo. The first ten customers she talked to told her that while they liked the shampoo, they found the packaging inconvenient. They could not hold their dog in the tub while trying to open the foil packet and squeeze the shampoo out. Katharine realized she had made a serious mistake in her choice of packaging, but now she had spent all her money and was

stuck with a large inventory of shampoo in foil packets. She did not know what else to do, so she closed her business.

Think Critically

1. What could Katharine have done to avoid her packaging mistake?
2. Is there anything Katharine could have done to avoid closing her business after she knew what the problem was?



© Getty Images/PhotoDisc

Research the target market before introducing a new product.

Every product has features. For instance, Luisa has many choices when she is deciding what types of olives to stock in her store. There are green and black olives and olives stuffed with pimientos, blue cheese, and almonds. There are olives that come in jars and in



© Getty Images/PhotoDisc

Why does Luisa need to offer a variety of cheeses and olives in her gourmet food store?

cans and fresh olives that are available loose. There are olives that are produced in the United States, in Italy, and in France. There are so many different types of olives that there is no way Luisa can offer every single type to her customers. She needs to decide how many types of olives she can carry and what kinds her target customer prefers.

Branding, Packaging, and Labeling

Making your product stand out from all the others in the market is a challenging task. **Branding** is the name, symbol, or design used to identify your product. The package is the box, container, or wrapper in which the product is placed. The label is where information about the product is given on the package. The brand, package, and label that you choose for your product will help differentiate it from others on the market. The Nike “swoosh” has become a very recognizable brand. When you see the Nike symbol, you know about the quality of the product you have selected.

Position Your Products or Services

Different products and services within the same category serve different customer needs. For example, both Hyundai and Jaguar sell automobiles, but these two product lines are positioned very differently in the marketplace. **Positioning** is creating an image for a product in the customer’s mind. Businesses position a product in a certain market to get a desired customer response. Product features, price, and quality may be used for positioning. Jaguar’s pricey cars are positioned in the market to meet the needs of those consumers who desire high quality and status. Hyundai positions its products to satisfy a need for an inexpensive family automobile. Examining the competition’s positioning

NETBookmark

What makes a memorable brand or product name? Access school.cengage.com/entrepreneur/ideas and click on the link for Chapter 5. Author Phillip Davis provides some thoughts in his e-zine article. What does Davis consider the most common naming mistake? Do you agree with him that “Apple” is a better brand name than something like “United Computer Manufacturers” or “Quality Computer Corporation”? Why or why not? Provide one example of a product or business that you think has a great name, and another that you think has a poor name. Explain your answers.

school.cengage.com/entrepreneur/ideas



strategy can help you determine the best positioning strategy for your target market.

Luisa knows that the other gourmet store in town is perceived as snobbish because it caters to professional cooks. Because of this, Luisa decides to position her store as the friendly gourmet store for anyone who loves to cook. To do so, she plans to offer in-store cooking classes and free samples of food items. She knows that being cheerful and helpful to customers will create and maintain her desired image.

Checkpoint

Why are product features, branding, and positioning important?

5.2 Assessment

THINK ABOUT IT

1. How can a small business use the marketing concept to its advantage over a larger business?
2. Choose one of your favorite products. Make a list of the features of the product.
3. In the blue jeans market, which brands are positioned to satisfy customers' need for high quality and status? Which brands are positioned to satisfy a need for inexpensive clothing? Describe the type of consumer who would buy each of the brands you name.

MAKE ACADEMIC CONNECTIONS

4. **RESEARCH** Choose a business in your community. Make a list of all the products and/or services it offers. Talk to the business owner about which of the products or services represent the largest revenue for the business. Find out which of the products or services are not profitable but are offered to customers as a convenience. Find out if the owner is thinking about adding any new products to the product mix or dropping some of the current products from the product mix and why.
5. **COMMUNICATION** You have created a new soft drink that is designed for students at your school. Design a label for the drink bottle that will brand the drink. You should incorporate your school's mascot in the design of the label.



TEAMWORK

Working with team members, make a list of products and services you would offer if you were opening a desktop publishing business. Make a list of the features of your products and services. Write a positioning statement that differentiates your business from your competitors.

5.3

The Marketing Mix—Price

Goals

- Identify pricing objectives for a business.
- Calculate the price for products using various methods.
- Discuss factors to consider when pricing services.
- List and describe various pricing techniques.

Terms

- return on investment
- market share
- demand-based pricing
- cost-based pricing
- competition-based pricing
- psychological pricing
- discount pricing

Focus on Small Business

What should I charge?

Marie was excited about her new business, “Straighten It Out,” which offered laundry services, such as washing and ironing clothes, for busy people. She would go to the homes of her clients once or twice a week and do all of their laundry for them. She liked the work and looked forward to the opportunity to make money while home from college. But, she was not sure how much she should charge for her services. She thought about charging a flat hourly rate. She realized that some of the tasks would take longer than others, and some would require extra care, such as having to treat stains, iron pleats, or handle delicates. An hourly rate might not be the fairest way to charge customers or the best way to earn money.

Work as a Team What do you think Marie should do? How should she decide how much to charge? What will happen if she charges too much? What if she charges too little?



Determine the best price for your product or service.

© Getty Images/PhotoDisc

Set Pricing Objectives

The price is the actual amount a customer pays for a product or service. Prices you charge must be low enough so that customers will buy from you, not from your competitors. To earn a profit, though, your prices need to be high enough so revenues exceed expenses. Before you can select a pricing strategy, you will need to establish objectives for your pricing program. What is the most important thing you want the price to do? Examples of pricing objectives include:

- Maximize sales
- Discourage competition
- Establish an image
- Increase profits
- Attract customers

Return on Investment

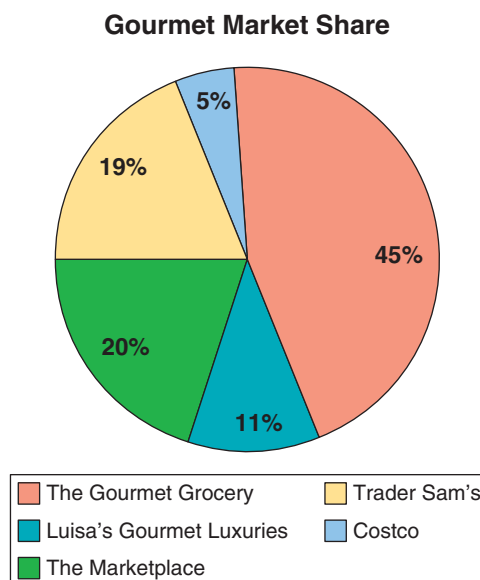
When setting pricing objectives, you may want to consider your return on investment. Investment refers to the costs of making and marketing a product. The **return on investment** (ROI) is the amount earned as a result of the investment, usually expressed as a percentage. Entrepreneurs must identify the percentage return they want from their investment. The target percentage in the beginning may be lower than it will be as the business grows. If you invest \$5,000 in your smoothie stand at a local park and you want a 15 percent return, you need to price your product so that you will earn \$750, since $\$5,000 \times 0.15 = \750 .

Market Share

Market share is another consideration when setting pricing objectives. **Market share** is a business's percentage of the total sales generated by all companies in the same market. The total market for a product must be known in order for a market share to be determined. For example, if people in Luisa's community normally spend \$1,750,000 a year on gourmet food products and Luisa's store sells products amounting to sales of \$192,500, her market share will be 11 percent, calculated as follows:

$$\begin{array}{rclcl} \text{Amount of sales} & \div & \text{Total market size} & = & \text{Market share} \\ \$192,500 & \div & \$1,750,000 & = & 11\% \end{array}$$

The chart below graphically illustrates Luisa's market share along with the expected market shares of her competitors.



Your market share will depend on the level of competition in your market. If you create a market for an entirely new product, your market share will be 100 percent because you will be the only supplier, at least for a period of time. If you enter a market with many competitors or one in which a few large companies dominate the market, your market share will be small at first.



© Digital Vision

How can networking contribute to a business's success?

Companies in highly competitive environments must develop a plan to gain a higher market share. Companies can increase market share in many ways. One way is to lower prices. Advertising and promotion campaigns that attract more customers can help too. You can also network with potential customers. Networking involves establishing informal ties with people who can help your business grow. Attending trade association meetings and other gatherings can give you good opportunities to network and gain new customers.

One of Luisa's goals is to become the most successful gourmet shop in her community by having a market share of at least 40 percent and a 10 percent return on investment. If Luisa wants a market share of 40 percent, she will need to generate annual sales of at least \$700,000. Based on this, Luisa sets her pricing objectives carefully. She decides to set her prices low to build customer traffic. Once Luisa has increased her market share, she may raise prices slightly to increase her return on investment.

To help increase her market share, Luisa will seek out networking opportunities. As part of her networking efforts, Luisa will play softball in a local women's league in the summer. She also plans to attend Chamber of Commerce meetings monthly. She hopes that through both settings she will meet people who will become customers. She also hopes to meet other business professionals, such as lawyers, financial advisers, and other business owners, who might offer advice on ways to run her business more efficiently, and in turn, increase her return on investment.

Checkpoint

Why is it important to determine pricing objectives before pricing goods and services?



Determine a Price for a Product

Once pricing objectives have been determined, the next step is to determine the possible prices for products. There will usually be more than one price that can be charged for a product. Pricing may be based on demand, cost, or the amount of competition.

Demand-Based Pricing

Pricing that is determined by how much customers are willing to pay for a product or service is called **demand-based pricing**. Potential customers are surveyed to find out what they would be willing to pay for the product. The highest price identified is the maximum price that can be charged.

If the bakery at Luisa's Gourmet Luxuries becomes widely recognized as the best in town, Luisa could begin charging higher prices for her baked goods. People will be willing to pay a higher price for a loaf of bread that they believe is the best available.

Cost-Based Pricing

Cost-based pricing is determined by using the wholesale cost of an item as the basis for the price charged. A *markup price* is a price determined by adding a percentage amount to the wholesale cost of an item. A *markdown price* is a price determined by subtracting a percentage amount from the retail price of an item.

Luisa buys artichoke hearts for \$1.77 a can. To cover her operating expenses and allow for a profit, she adds 40 percent to her wholesale cost, or \$0.71. The new price of \$2.48 is her retail price.

$$\begin{array}{rclcl} \text{Wholesale cost} & \times & \text{Percentage markup} & = & \text{Markup amount} \\ \$1.77 & \times & 0.40 & = & \$0.71 \end{array}$$

$$\begin{array}{rclcl} \text{Wholesale cost} & + & \text{Markup amount} & = & \text{Retail price} \\ \$1.77 & + & \$0.71 & = & \$2.48 \end{array}$$

Sometimes business owners purchase too much of a particular item and want to sell more of it quickly. To do so, they mark down the retail price of the product. You should be careful not to mark down an item below its cost. You do not want to lose money.

Luisa usually charges \$10.50 for a large bottle of olive oil. To sell more, she decides to mark down its retail price by 20 percent.

$$\begin{array}{rclcl} \text{Retail price} & \times & \text{Percentage markdown} & = & \text{Markdown amount} \\ \$10.50 & \times & 0.20 & = & \$2.10 \end{array}$$

$$\begin{array}{rclcl} \text{Retail price} & - & \text{Markdown amount} & = & \text{Markdown price} \\ \$10.50 & - & \$2.10 & = & \$8.40 \end{array}$$

Competition-Based Pricing

Pricing that is determined by considering what competitors charge for the same good or service is called **competition-based pricing**. Once you find out what your competition charges for an item, you must decide whether to charge the same price, slightly more, or slightly less.





What things should Luisa consider when competing against another grocer that is already well established in her community?

Luisa's business will compete with The Gourmet Grocery, which has been in her community for five years. She cannot charge more than her competitor for items that customers could purchase there. She decides initially to charge a few cents less than The Gourmet Grocery on all packaged goods. She will keep an eye on competitors to make sure she stays up to date on what they are charging for their products.

Checkpoint

List three methods for determining the price to charge for a product.

Price a Service

When setting the price for a service, it is important to consider not only the cost of any items used in providing the service, but also the amount of time and anything that is included with the service.

Time-Based Pricing

The price to charge for services can be determined by the amount of time it takes to complete the service. A plumber may charge \$100 per hour. If the job takes 1½ hours to complete, the labor charge would be $\$100 \times 1.5 = \150 . A service provider must decide whether there will be a separate charge for materials or whether the materials will be included. A hair stylist charges a set amount to highlight someone's hair. The amount includes the hair stylist's time as well as all of the supplies used for the highlighting. Some service providers will negotiate the price. This is often done with legal services and construction projects.

One area in which Luisa would like to expand her business is catering. She will have to calculate prices based not only on the cost of the food but also on the time that it takes for her to prepare and deliver the food. If she is responsible for serving at a catered event,



she will have to charge for her time and the time of any helpers she may hire to wait on the guests at the event.

Bundling

Services can be *bundled*, or combined under one price, rather than making the customer pay for each individual part of the service. Airlines use bundling when they charge a passenger for a ticket. The price includes not only the transportation, but also any food and beverages served, the services of the employees who check in passengers, and baggage handling.

Checkpoint

Which method would be the best for a housepainter to use to price services? Why?

Pricing Techniques

It is important to set the right price for your products and services. Pricing can make or break a business. When first introducing a product or service into the market, price skimming and penetration pricing techniques may be used. Afterwards, psychological pricing and discount pricing are two pricing techniques that you should examine and incorporate when establishing permanent pricing for your products and services.

Introductory Pricing

As a product is introduced into the market, sales will be low, marketing costs will be high, and little if any profit will be made. Two pricing techniques that are often used in the introductory stage of a product are price skimming and penetration pricing. *Price skimming* is used when a product is new and unique. A high price is charged to recover the costs involved in developing the product. Then as more competitors enter the market with similar products, the price is dropped. *Penetration pricing* starts out with a low

introductory price with the goal of building a strong customer base. The low price also discourages competition.

Psychological Pricing

Psychological pricing is based on the belief that certain prices have an impact on how customers perceive a product. This type of pricing is most often used by retail businesses. Techniques used in psychological pricing include the following:

- *Prestige pricing* is selling at a high price in order to create a feeling of superior quality and social status.

BE YOUR OWN BOSS

You plan to open a pizza delivery service near the University of Florida in Gainesville. Your target market includes students who live in dorms and houses on and near the main campus. You know that the price you charge is going to be critical to the success of your business as there are several restaurants in the area with which you will be competing. Develop a psychological pricing strategy for the pizza delivery service.



© Getty Images/PhotoDisc

How does price affect your buying behavior?

- *Odd/even pricing* suggests that buyers are more sensitive to certain ending numbers. Studies have shown that prices ending in odd numbers are perceived to be bargains while those ending in even numbers suggest higher quality. For example, \$29.99 sounds like a bargain compared to an even \$30.00.
- *Price lining* involves offering different levels of prices for a specific category of product based on features and quality. A jeweler might offer three price lines of diamond necklaces and display them in different cases so that shoppers can go straight to the price level they can afford.
- *Promotional pricing* is offering lower prices for a limited time to increase sales. This type of pricing is temporary and prices will return to normal when the promotion ends.
- *Multiple-unit pricing* involves pricing items in multiples, such as 10 for \$10. This type of pricing suggests a bargain. People will buy more items than they would if they were priced individually.

Discount Pricing

Discount pricing offers customers a reduced price. Discount pricing is used to encourage customers to buy. Markdowns are a type of discount pricing. Other discount pricing strategies include the following:

- *Cash discounts* are offered to customers to encourage early payment of invoices. When this is done, the terms of an invoice will include the amount of the discount, the number of days in the discount period, and when the invoice is due if the discount is not taken. For example, terms of “2/10, net 30” mean that a 2 percent discount may be taken if the invoice is paid within 10 days. If no discount is taken, the net or total amount of the invoice is due within 30 days of the date of the invoice. To find the last date available for the discount, add the number of days in the discount period to the date of the invoice. If the invoice is dated April 1, you would add 10, and the last day of the discount period would be April 11.



- *Quantity discounts* are reductions in price based on the purchase of a large quantity. This is also called a volume discount. Sellers offer quantity discounts because it reduces their selling expenses.
- *Trade discounts* are reductions on the list price granted by a manufacturer or wholesaler to buyers in the same trade.
- *Seasonal discounts* are used for selling seasonal merchandise out of season. Barbeque grills are in high demand in the spring and summer months, but not in the fall and winter. Manufacturers offer discounts to customers who purchase grills out of season.

Checkpoint

Name two techniques used in psychological pricing and provide an example of each.

5.3 Assessment

THINK ABOUT IT

1. What pricing objectives are most important to a new business?
2. What do you need to consider when pricing services?
3. Why is discount pricing used?

MAKE ACADEMIC CONNECTIONS

4. **COMMUNICATION** Look through advertisements in newspapers and magazines and find examples of psychological pricing. Prepare a poster of the advertisements and label each pricing technique.
5. **MATH** You have a large inventory of small appliances in your kitchen store that have not sold during the past year. You decide to mark them down by 30 percent each. Using the Activity CD, open the activity "Pricing Products." Calculate the markdown price for each item. After two weeks, you still have some of these items, so you decide to mark them down an additional 25 percent off. Find the new markdown price.



TEAMWORK



You and your teammates are going to open a home entertainment store. Using the Activity CD, open the activity "Home Entertainment Store." Print a copy and complete the activity. Locate distributors, wholesalers, and manufacturers of three products you would like to sell. Choose at least two brands for each item. Contact the distributor to obtain information about pricing and delivery. What is the wholesale price of each product? Find the same product in a local store. What is the retail price? What is the markup percentage?



Sharpen Your Entrepreneurial Skills

Breakeven Point

As an entrepreneur, you will have to make decisions about pricing your products. Knowing how to calculate the breakeven price will help you ensure you do not price products below your cost. You do not want to lose money!

The lowest price identified in a price range is based on the costs of the product to the seller. All production, marketing, and administrative costs should be considered when determining the minimum price. The minimum price can be calculated through breakeven analysis. The breakeven point is the point at which sales revenue equals the total cost of acquiring/producing and selling a product or service. At the breakeven point, a business has no profit and no loss—it simply breaks even. A business can use the breakeven point in units to analyze whether it is charging an appropriate price.

To calculate the breakeven point in units, a business must determine the selling price, fixed costs, and variable costs for one unit. Then, total fixed costs are divided by the selling price minus the variable costs.

Luisa's Gourmet Luxuries sells stainless steel pasta pots. Luisa determines that her fixed costs are \$35,000 a year and her variable costs per unit are \$9. Luisa wants to determine how many pasta pots she would have to sell to break even if the price is set at \$150. Her breakeven point for the pasta pots would be calculated as follows:

$$\begin{array}{rcllcl} \text{Total fixed costs} & \div & (\text{Selling price} - \text{Variable cost}) & = & \text{Breakeven point} \\ \$35,000 & \div & (\$150 - \$9) & = & 248.2 \end{array}$$

The breakeven point in units would be approximately 249 units. Luisa must determine if she can sell 249 pasta pots. If she can, she can set the price at \$150. If she wants to make a profit on the pasta pots, she will have to sell more than 249 units. Luisa can make additional calculations to determine the relationship between price and breakeven point.

TRY IT OUT

You own AAA Audio/Video Repair. You make service calls to customers' homes to repair their audio/video equipment such as television sets and home theater systems. Your fixed costs are \$10,000 a year and your variable costs for each service call are \$20. If you charge \$75 for each service call, how many service calls will you have to make in order to break even?



© Digital Vision

Chapter 5 | Assessment

SUMMARY

5.1 Develop the Marketing Plan

1. Marketing is all of the processes—planning, pricing, promoting, distributing, and selling—used to determine and satisfy the needs of customers and the company. Businesses that follow the marketing concept use the needs of customers as the primary focus. You must determine the right marketing mix—the blending of product, price, distribution, and promotion—to use to reach your target market.
2. A marketing strategy identifies how you will achieve your marketing goals. For a new business, a marketing strategy should address, product introduction or innovation, pricing, distribution, promotion, sales or market share, and projected profitability.
3. A marketing plan should include information on the product or service, target market, competition, marketing budget, business location, pricing strategy, promotional strategy, and distribution strategy. Putting it in writing helps you determine whether your marketing plan is solid and all parts are consistent.

5.2 The Marketing Mix—Product

4. The different products and services a business offers are its product mix. The marketing concept keeps you focused on meeting the wants and needs of customers as you develop a product mix.
5. Product features are the characteristics of the product that will satisfy customer needs. Branding is the name, symbol, or design that identifies your product. The brand, package, and label will differentiate your product from others. Positioning is creating an image for a product in the customer's mind.

5.3 The Marketing Mix—Price

6. A business may set pricing objectives aimed at maximizing sales, increasing profits, discouraging competition, attracting customers, or maintaining an image.
7. Pricing may be based on demand, cost, or competition.
8. Services may be priced based on time, materials used, and bundling.
9. Introductory pricing techniques include price skimming and penetration pricing. Psychological pricing techniques include prestige pricing, odd/even pricing, price lining, promotional pricing, and multiple-unit pricing. Discount pricing includes cash discounts for paying early, quantity discounts, trade discounts, and seasonal discounts.

What do you know now?

Read Ideas in Action on page 119 again. Then answer the questions a second time. How have your responses changed?

VOCABULARY BUILDER

Match each statement with the term that best defines it. Some terms may not be used.

1. All of the processes—planning, pricing, promoting, distributing, and selling—used to determine and satisfy the needs of customers and the company
2. Uses the needs of customers as the primary focus during the planning, production, distribution, and promotion of a product or service
3. A blending of product, price, distribution, and promotion used to reach a target market
4. Identifies how marketing goals will be achieved
5. Amount earned as a result of an investment
6. Product characteristics that satisfy customer needs
7. The name, symbol, or design used to identify your product
8. A business's percentage of total sales generated by all companies in the same market
9. Creating an image of a product in the customer's mind
10. The different products and services a business sells
11. Pricing that is determined by how much customers are willing to pay for a product or service
12. Pricing that is determined by using the wholesale cost of an item as the basis for the price charged
13. Pricing that is based on the belief that certain prices have an impact on how customers perceive a product
14. Pricing that offers customers a reduced price to encourage them to buy

- a. branding
- b. competition-based pricing
- c. cost-based pricing
- d. demand-based pricing
- e. discount pricing
- f. features
- g. market share
- h. marketing
- i. marketing concept
- j. marketing mix
- k. marketing plan
- l. marketing strategy
- m. positioning
- n. product mix
- o. psychological pricing
- p. return on investment

REVIEW YOUR KNOWLEDGE

15. To successfully use the marketing concept, a business must do which of the following?
 - a. identify what will satisfy the customers' needs and wants
 - b. develop and market products or services that customers consider better than other choices
 - c. operate profitably
 - d. all of the above
16. List six elements that should be addressed in a company's marketing strategy.
17. A marketing strategy should be consistent with the business's ____? ____.
18. **True or False?** Opening two more restaurants in other locations around the city would be an example of a short-term goal for the owner of a new restaurant.
19. Which of the following would be a good addition to the product mix for a health club?

a. diamond rings	c. fitness apparel
b. chocolate-chip cookies	d. photo print service

20. The branding, packaging, and labeling of your product should accomplish all of the following *except*
 - a. identify your product
 - b. describe the company's product mix
 - c. differentiate your product from others on the market
 - d. provide information about the product
21. Which of the following is *not* a pricing objective?
 - a. to maximize sales
 - b. to increase profits
 - c. to attract customers
 - d. to decrease expenses
22. A new cellular phone that lets you watch television, surf the Internet, send and receive e-mail, take pictures, and listen to music has just been released. There are people who want this device so badly they are willing to pay any price for it. This telephone should be priced using
 - a. demand-based pricing
 - b. cost-based pricing
 - c. competition-based pricing
 - d. time-based pricing
23. During late summer, Nordstrom's Department Store offers fall and winter clothes at a discounted price for a short period of time. After that time, the price of this clothing goes up and is not reduced again until the end-of-season clearance. This is an example of
 - a. prestige pricing
 - b. price lining
 - c. promotional pricing
 - d. multiple-unit pricing
24. You own an office supply store. You purchase desk lamps at a wholesale cost of \$14 each. You use a markup of 45 percent to determine the retail price? At the end of season, you offer a discount price using a markdown of 20 percent of the retail price. The discount price for desk lamps is
 - a. \$20.30
 - b. \$17.50
 - c. \$16.24
 - d. \$11.20
25. Which of the following pricing techniques is often used when introducing a new product into the market with the goal of developing a strong customer base while discouraging competition?
 - a. price skimming
 - b. penetration pricing
 - c. prestige pricing
 - d. price lining

APPLY WHAT YOU LEARNED

26. You want to open a gardening business. You plan to offer planting, weed pulling, and watering services to busy homeowners in your neighborhood. Write a positioning statement for your business.
27. Look for advertisements containing pricing information. Identify the pricing strategy you think is being used in each ad and explain why.

MAKE ACADEMIC CONNECTIONS

28. **MATH** The annual sales of home entertainment equipment in your area is \$23 million. You want to capture 15 percent of the market. How much will you have to sell to achieve your goal?
29. **COMMUNICATION** Write a paragraph describing how psychological pricing has affected one of your purchasing decisions.

30. **PROBLEM SOLVING** Your sporting goods store sells fitness equipment. Included in your product mix is a treadmill that is not selling well, and you do not understand why. List some possible causes. Outline strategies for determining the reason behind low sales.
31. **MATH** You want to download some special relaxation music that you will play in the nail salon you are going to open. The site that you download music from is offering a multiple-unit price on music downloads this month. For every 3 songs you download, you pay only \$2.50. If you download only one or two songs, the price is \$0.99 per song. You download 38 songs. How much will you have to pay for the downloads?

WHAT WOULD YOU DO?

You offer a math tutoring service for children at the elementary and middle schools in your neighborhood. You normally charge \$15 per hour. You recently received a message from the mother of a fifth grader inquiring about your services and pricing. She got your name from the mother of another student you tutor. You recognize her name as being from a family who owns a very large business in your town. You would like to charge her more than \$15 per hour because you know the family is wealthy.

What would you do? Is it fair for you to raise your price just because you know the family has more money? What problems do you think you might experience if you charge customers different prices? Under what circumstances would you be justified in charging customers different prices?

BUILD YOUR Business Plan *Project*

This activity will help you get started on the development of a marketing plan for your business idea.

1. Define short-, medium-, and long-term marketing goals for your business.
2. Determine the product mix for your business and the features of each product. How do you plan on positioning your products?
3. Decide how you will develop brand recognition for your business. Design any logos, symbols, and/or product labeling and packaging you will use.
4. Determine your pricing objectives and how you plan to achieve them.
5. Develop a pricing strategy for your products and/or services. What price will you charge? How did you decide on this price?
6. Calculate the breakeven point based on your selling price. Is your breakeven point realistic? Do you need to adjust the selling price?

Planning a Career in E-marketing



"My boss gave me one hour to surf the Web to research a potential business he might develop. The time limit was to encourage me to stay focused. Each web site had multiple links to other sites. Some sites had movie-quality commercials, some sites offered free products, and some sites distracted me with banner ads and pop-ups. When the hour was up, my summary report included the assigned topic and additional information about related topics."

Why do web sites contain links to other sites? Why are some web sites easier to navigate than others?

E-marketing is an expanding field that helps companies reach consumers via the Internet. Web site designers help companies and organizations develop web sites that inform potential customers about products and services offered.

EMPLOYMENT OUTLOOK

- Faster than average growth is anticipated.
- As businesses increase their dependence on the Internet for the efficient distribution of product and marketing information, demand for these jobs will continue to grow.

JOB TITLES

- Online Marketing and Outreach Coordinator
- Web Site Template Designer
- Web Page Developer
- Portal Designer
- Web Site Marketer

NEEDED SKILLS

- A Bachelor's degree is recommended.
- Strong problem-solving and analytical skills are required.

- Computer science and business courses are helpful.
- Experience in content management, HTML, and assorted web-related software is required.

What's it like to work in E-marketing?

This morning Lev, a freelance web site designer, is meeting with a small group of investors who want to build a dozen windmills on property bordering a huge lake. As part of a public relations campaign to encourage community support for the project, the investors want to develop a web site about the project. Lev has been contracted to develop a web site that will list all of the benefits of the windmill farm. The web site needs to include photos of the windmill farm's proposed design, statistics on the amount of homes that can be powered from wind energy, and data reflecting flight patterns of local birds. The site also needs to provide links to similar small-scale projects that have been successful.

In the afternoon, Lev will meet with a farmer's association that wants to provide support via a web site for independent farmers who want to convert corn to ethanol. This meeting will focus on the site's content and possible links to other informational sites. In addition, the group will be making design decisions related to color, icon graphics, and editorial style. Navigation models will also be considered. To help make the project more appealing to farmers, Lev must ensure that the web site is easy to navigate.

What about you? Would you like to design web sites that are informative, easy to navigate, and profitable for their sponsors?



GLOBAL MARKETING TEAM EVENT

Teams will develop a written international marketing plan that identifies the customer base. The participating team must demonstrate oral communication skills to market a new product. The written marketing plan must not exceed ten pages. The completed written plan must include the Title Page; Table of Contents; Synopsis; Company Goals; Description of Customers and Their Needs; Description of Pricing Strategy; Competition; Marketing Mix; Economic, Social, Legal, and Technological Trends; Human Resource Requirements; Marketing Timeline; Methods of Measuring Success; and Supporting Documentation. BPA selects a new topic for the Global Marketing Team Event every year.

TOPIC You are the Marketing Director for Flower Power. Your flower farm, located in southern Texas, raises fresh, reasonably-priced flowers that are sold throughout the United States. Most of your customers are wholesalers and supermarkets. Research indicates that the global economy offers numerous markets for your fresh flowers. Your company has recently developed a revolutionary packaging system that will ensure the delivery of fresh flowers to international customers. The package also meets all international standards, making it more likely to clear another country's customs, which are restrictions imposed on imported products.

Your presentation must explain your marketing plan for conducting business globally.

PERFORMANCE INDICATORS EVALUATED

- Demonstrate knowledge and understanding of management and international business concepts.
- Communicate research in a clear and concise manner, both orally and in writing.
- Demonstrate teamwork skills needed to function in a global marketing environment.
- Demonstrate successful price selection methods.
- Demonstrate effective persuasive and informative communication and presentation skills.

Go to the BPA web site for more detailed information.

Think Critically

1. Why is the packaging so important for fresh-cut flowers?
2. Why is it important for the product to clear customs?
3. Why must Flower Power understand customs (cultural traditions) in other countries?
4. Why are the packaging costs important in this case?

www.bpa.org

Chapter 6

© Digital Vision



Distribution, Promotion, and Selling

6.1 The Marketing
Mix—Distribution

6.2 The Marketing
Mix—Promotion

6.3 Selling and
Promoting

school.cengage.com/entrepreneur/ideas

IDEAS IN ACTION

Turning a Bad Experience into a Million Dollars

Can you imagine being 15 years old and a guest on the *Oprah Winfrey Show*? Being featured on an *ABC News Special*? Or being the CEO of your own company and well on your way to your first million dollars? That's exactly what has been going on in Jasmine Lawrence's life lately. Jasmine, from Mt. Laurel, New Jersey, is the CEO of Eden Body Works—a company she was inspired to create at 11 years of age because of a bad experience with a hair product.



© Euan Henry

Jasmine Lawrence Eden
Body Works

Jasmine used a chemical relaxer on her hair when she was 11 that caused her to lose much of her hair. She decided that she would never use harsh chemicals on her hair again and began conducting research on all-natural ingredients. She used the Internet and consulted with hair-care specialists to find out what it takes to keep hair healthy. She conducted multicultural focus groups made up of both men and women. Then she began experimenting with mixing her own hair oils, shampoos, and conditioners. Soon friends and family members were asking her for products.

At the age of 12, Jasmine prepared for entrepreneurship by attending a Biz Camp sponsored by the National Foundation for Teaching Entrepreneurship. During the next year, she developed a business plan, filed a trade name certification with the state of New Jersey, and opened her business. Jasmine's leadership has led to a tremendous amount of growth.

As Eden Body Works has grown and increased its customer base, Jasmine's distribution channels have also changed. Initially she sold directly to customers and promoted products through a company web site. Gradually she began working through retailers as beauty/braiding salons and barbershops began to both use and carry her products for resale to their customers. Then some Whole Foods Stores began carrying her products. Most recently, Jasmine struck a deal with Wal-Mart to begin offering her products. Jasmine's motivation to start her own business was driven from her own needs. Today, she is the manufacturer, the wholesaler, as well as a consumer of her own products.

What do you know?

1. Do you think Jasmine's research on the needs of healthy hair contributed to the success of Eden Body Works?
2. Describe how using different distribution methods have helped Jasmine's business to grow.
3. Do you think the publicity that Jasmine has received has contributed to the growth of Eden Body Works?

6.1

The Marketing Mix—Distribution

Goals

- Describe the four basic options of channels of distribution.
- Apply channels of distribution to the specific needs of various types of businesses.
- List factors to consider in the physical distribution of products.

Terms

- distribution
- channels of distribution
- direct channel
- indirect channel
- physical distribution

Focus on Small Business

Distribution mixup

Dustin owns a small hardware store in south Florida. During the winter, he placed an order for swimming pool supplies to be delivered in early spring. He knew that pool usage and maintenance needs would increase for his customers in the spring. He wanted to be sure he had everything they needed. His supplier processed the order and assured Dustin it would be delivered in late February. Imagine Dustin's surprise when he opened the box from the supplier and found a product used to melt snow on walkways and driveways!

Work as a Team What do you think happened to Dustin's order? What is the problem here? How do you think Dustin should handle this situation?



Distribution problems can negatively impact a business.

© Digital Vision

Channels of Distribution

Distribution is an important component of the marketing mix that involves the locations and methods used to make products available to customers. As you develop a distribution strategy for your business, you will determine how you will get your goods and services to your customers. You must be sure you have the right product in the right place at the right time.

Luisa Ramirez, who is opening a gourmet food shop and catering business in her community, knows that she must consider distribution in the marketing of her business. She will need to consider how to get the goods to sell, as well as how to actually get them into the customers' hands.

Channels of distribution are the routes that products and services take from the time they are produced to the time they are consumed. Choosing the right channel of distribution for a product includes finding the most efficient way to ship it to desired locations. Using the right distribution channels means saved time and lower costs for both buyers and sellers.

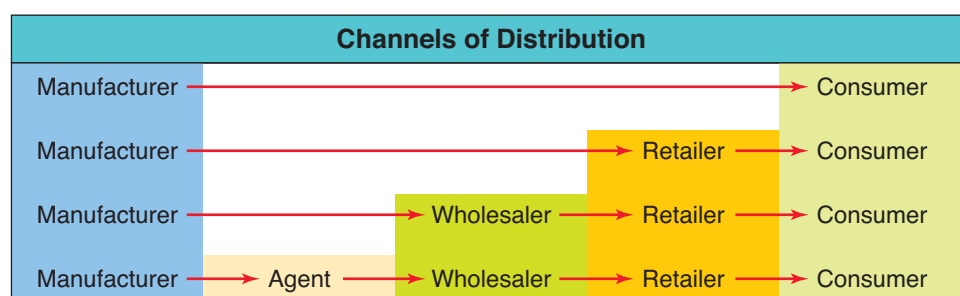
Direct and Indirect Channels

Channels are either direct or indirect. A **direct channel** moves the product directly from the manufacturer to the consumer. An **indirect channel** uses *intermediaries*—people or businesses that move products between the manufacturer and the consumer. Agents and wholesalers serve as intermediaries.

Getting a product to the market in a timely manner is an important component of the distribution phase. If a farmer in South Georgia grows strawberries, the value of the strawberries will be maximized if they can be moved to northern markets quickly while they are fresh. Because there is a lack of fresh strawberries in northern markets, they will command a better price based on higher demand. The strawberry farmer must determine whether to use a direct or indirect channel of distribution to get the product to customers.

Channel Options

Entrepreneurs should examine the different options for channels of distribution and choose the one that best meets the needs of their business. The four basic options are illustrated and described below.



- 1. Manufacturer to Consumer** The product can be sold by the manufacturer directly to the consumer through the Internet, direct mail, or television shopping channels. There are no intermediaries involved in this option, and it is the most cost-effective. However, sales opportunities are limited because it is more difficult for a manufacturer to reach the final consumer.
- 2. Manufacturer to Retailer to Consumer** A sales force can sell manufactured goods to retail stores, and the retail stores can sell to the consumers. This is a more expensive option than selling directly from the manufacturer to the consumer, but it offers more sales opportunities.
- 3. Manufacturer to Wholesaler to Retailer to Consumer** To reach a large market, the manufacturer can sell large quantities to a wholesaler who will then store and sell smaller quantities to many retailers. Even though more intermediaries are involved in this method, prices can be lower because the manufacturer is producing mass quantities of the product, resulting in lower production costs.

Develop Your Reading Skills

List all of the chapter key terms on the board. Have students write a definition for each key term before reading the chapter. When a key term is introduced in the chapter, have students compare the definition to the one they wrote and correct their definitions as needed.



- 4. Manufacturer to Agent to Wholesaler to Retailer to Consumer**
 With this option, the manufacturer does not get involved in selling. Selling is handled by an agent. This option is often chosen by manufacturers involved in international marketing.

Checkpoint

What are the four basic options of channels of distribution?

Distribute Goods and Services

Retail businesses, service businesses, and manufacturing businesses will choose different channels of distribution based on the needs of their businesses. In addition, all types of businesses must carefully plan their distribution strategy to ensure customer satisfaction.

Retail Businesses

Retail businesses have many ways of selling products. As the owner of a retail business, you can distribute products in various ways.

- Offer your product or service to consumers in a convenient location and during convenient hours.
- Use catalogs, fliers, and other advertisements to reach customers who live outside the area. Take orders by phone or fax and ship them directly to customers.
- Create a web site. People with access to the Internet can visit your web site to learn about your products and services and to make online purchases.

Luisa's food and catering shop is a neighborhood business that caters to local residents, so she does not think she would get much benefit from catalogs. As a convenience for customers, Luisa decides to stay open until 8:00 on weeknights and have hours from 10:00 until 4:00 on Saturdays and 12:00 to 4:00 on Sundays. She also creates a web site that contains product descriptions, menus, and order forms for customers wanting to place catering orders.

BE YOUR OWN BOSS

You plan to open a kite shop in a beach resort town. You will sell custom-made kites as well as kites you plan to import. You know that you will have customers during the spring and summer when families are visiting the beach, but you are looking for ways to increase sales during the off-season when there are very few visitors to the area. Describe ways that you could distribute your products that would increase sales during the off-season.

Service Businesses

Most entrepreneurs who own service businesses sell their services directly to customers. These businesses have a single, direct channel of distribution because the production and consumption of a service happens at the same time. For example, electricians, restaurant owners, and lawyers deal directly with the people who purchase their services. It is important for a service

provider to offer the service when it is needed by the customer to maximize the value of the service. If the service cannot be provided when needed, the customer will look for another provider. Some service businesses, such as film developers, use retail stores to distribute their services.

Manufacturing Businesses

Manufacturers usually don't sell directly to customers. Instead, they make their products and then sell the products to other businesses, such as retailers. The retail store then sells to the final consumer.

Some manufacturers distribute their products very broadly and use all possible channels of distribution. Other manufacturers distribute their products through selected outlets only. For example, high-priced cosmetics usually are sold in exclusive department stores. Inexpensive cosmetics are sold in discount stores and drugstores.

Checkpoint

Why are channels of distribution different for different types of businesses?

Physical Distribution

Physical distribution includes not only transportation but also storage, handling, and packaging of products within a channel of distribution. A product may move through several channel members by various forms of transportation to get it to the point where it will ultimately be sold to consumers. As the product is transported, it will be stored at various points along the channel as paperwork is processed and it is moved to the next channel member. It is important for storage facilities along the channel to be adequate and safe to protect the product.



© Digital Vision

How can you determine the best method for transporting goods?

Transportation

There are many choices when transporting goods. Products can be moved by airplane, pipeline, railroad, ship, truck, or a combination of methods. You must determine which method is best and most cost-efficient for your products. Factors to consider in making a transportation decision include what you are shipping and where it is being shipped. If you are shipping a small product to someone in your city, you would probably choose a parcel delivery service. If you are shipping a large item to another country, you would probably send the item by ship or



air and use a truck to get the product to and from the shipyard or airport. If the product is perishable, you may need to choose a carrier that provides refrigeration or that can move the product very quickly to its destination.

Product Storage and Handling

Efficient storage allows channel members to balance supply and demand of products. However, this adds to the cost of the products and also adds the risk that products may be damaged or stolen while stored. Most products are stored in warehouses at various points through the channels of distribution. An automobile manufacturer in Japan selling autos in the United States stores them in Japan at the factory and at the shipyard until they are shipped. Once they arrive in the United States, they will be stored at the port until they can be loaded onto automobile carriers to be distributed to the dealers. Dealers have to provide storage for the automobiles until they are sold to the consumer.

Packaging

Packaging is designed to protect the product from the time it is produced until it is consumed. If the product is not protected during the distribution phase, it could be damaged or destroyed, resulting in a loss of money to channel members. Packaging requirements will vary depending on the product, the way it is shipped, and where it is being shipped. The auto manufacturer in Japan packages a small accessory item being shipped to the United States differently than the autos it ships.

Receiving Goods to Sell

All types of businesses must receive goods from suppliers. Whether or not they sell goods to customers, all businesses need paper, computers, raw materials, and more to be able to function. Retailing businesses need to obtain goods to sell. A service business that grooms pets needs to buy cat and dog shampoos and flea combs. A blanket manufacturer must buy cotton.



© Digital Vision

Why does physical distribution play an important role for retail stores?

You can use various sources to locate distributors, wholesalers, and manufacturers. Your public library and the Internet will have research materials you can use. Some helpful sources include the following:

- *The American Wholesalers and Distributors Directory*, which lists suppliers in a wide range of industries
- *The Thomas Register*, which lists all manufacturing companies
- Trade magazines that may include articles about or advertisements for suppliers in your industry

Luisa needs to create relationships with wholesale distributors. She must find companies she can trust to deliver high-quality products quickly. Luisa will purchase products directly from companies that produce them and through distributors. Her pastries come from a local baker. Distributors will supply her with imported and domestic canned goods, as well as meat, fruits, and vegetables.

Checkpoint

What factors are important to consider in the physical distribution of products?

6.1 Assessment

THINK ABOUT IT

1. Which channel of distribution would be the best for a dairy farm with limited production of a few products to be sold to a small group of local customers?
2. How does distribution add value to goods, services, and ideas being sold?
3. How is it possible to add intermediaries to the distribution channel and at the same time increase profits?

MAKE ACADEMIC CONNECTIONS

4. **GEOGRAPHY** Think of a product that would have to be shipped from another country to the United States. Research the route that the product would follow while being shipped. Write a paragraph describing the places the product would pass through and describe the method of transportation that would be used for shipping.
5. **COMMUNICATION** Make a list of products that are sold directly to consumers by the manufacturer. Share the list with your classmates.



TEAMWORK

Working in a team, choose one of the following products: apples, MP3 players, magazines, milk, motor oil, t-shirts, CDs, or DVDs. Draw flow charts tracing all the channels of distribution possible for the product.



6.2

The Marketing Mix—Promotion

Goals

- List the many forms of advertising and discuss advantages and disadvantages of each.
- Define publicity and describe ways to use publicity as a promotional tool.

Terms

- advertising
- publicity
- press release
- public relations

Focus on Small Business

The costs of promotion

From the moment she got the idea to open her own spa, all Chachi could think about was Grand Opening Day! But she knew that there were many things to do before she was ready to open. She took her time and worked through all the details, preparing her business plan and securing financing for the business. Now Chachi is ready to get the word out to her target market. She wants to be sure that the information she shares gives customers a reason to want to visit the spa. She considers offering a free spa service with the purchase of a spa service on opening day. This promotion could cost her up to \$120 per free service. Chachi has a staff of four, but only two of them are certified to perform certain spa services. So she knows she must consider any staffing problems that could occur on opening day as a result of the promotion.

Work as a Team Do you think Chachi's idea for an opening day promotion is a good one? Why or why not? Can you suggest some alternative promotions that Chachi might use?



© Getty Images/PhotoDisc

There are many factors to consider when developing promotions.

Promotion Strategies

No matter how wonderful your products, distribution methods, and pricing, you will not succeed as an entrepreneur if customers do not know about your business. You will have to promote your business to make customers aware of the benefits of buying from you. Promotion takes many forms, including advertising, publicity, personal selling, and sales promotion. The strategy created by adopting a blend of some, if not all, of these techniques is called your *promotional mix*.

Advertising

Service industries, manufacturers, and retailers all advertise. **Advertising** is a paid form of communication sent out by a business about a product

or service. It keeps your product or service in the public's eye by creating a sense of awareness. Advertising should help a business convey a positive image.

Advertising can be very important for small businesses, particularly new ones. Advertising helps you communicate with potential customers. It lets them know what kinds of products and services your company offers and why they should buy from you.

Large companies generally use advertising agencies to create their advertisements. Using an advertising agency usually results in highly creative and effective ads, but it can be very costly. As an owner of a small business, you probably will handle your own advertising.

CHOOSE YOUR MESSAGE Your advertising should clearly communicate the message and image you want. If, for example, your marketing strategy is to have low prices, advertisements highlighting your prices might be appropriate. If your aim is to target customers who are willing to pay higher prices for excellent service, advertising that describes your well-trained staff would fit your image.

Once you choose a message, you will need to decide which advertising medium to use. To choose a medium, you will have to consider both cost and effectiveness in reaching your target audience.

Online Advertising

As Internet use has increased, online advertising has become widely used by businesses to promote their products and services. This is a cost-effective way for businesses to get information to potential customers. Ongoing changes and advancements in online advertising technology make it easier for customers to get the information they need. Potential customers can use keyword searches and browse through online catalogs by category to find information about available products and services.

Online technology lets businesses interact with customers through online chat rooms, blogs, and e-newsletters. A well-designed web site can enhance customers' experience by giving them easy-to-navigate pages that contain up-to-date information on products and services.

TYPES OF ONLINE ADVERTISING Online advertising combines color, imagery, animation, and other elements to attract the reader's attention. Some common types of online advertising include the following:

- **Banner Ad** A graphic image or animation displayed within a rectangular box across the top or down the side of a web page
- **Floating Ad** An ad which moves across the screen or floats above the page content
- **Wallpaper Ad** An ad which changes the background of the page being viewed
- **Trick Banner** A banner ad that looks like a dialog box with buttons, often appearing like an error message or an alert
- **Pop-Up Ad** A new window that opens in front of the current one, displaying an advertisement

did you KNOW?

In 2006, the top 10 advertisers spent over \$18 billion combined. The top 10 spenders were as follows:

- Procter & Gamble
- General Motors
- AT&T Inc.
- Verizon
- Time Warner Inc.
- Ford Motor Co.
- Walt Disney Co.
- DaimlerChrysler
- Johnson & Johnson
- News Corp.



- **Pop-Under Ad** Similar to a pop-up ad except that it loads behind the current window and does not appear until the user closes one or more active windows

PAYING FOR ONLINE ADVERTISING Determining the effectiveness of online advertising is more accurate than other forms of traditional advertising. As a result, new methods of charging for online advertising have been developed, based on the effectiveness of the ads. Three of the most common ways online advertising is purchased are as follows:

- **Cost per Mil (CPM)** The charge to the advertiser is based on the exposure of the message to a specific audience. CPM costs are priced per thousand viewers reached with the message.
- **Cost per Click (CPC)** The charge to the advertiser is based on the number of user clicks on the advertisement. This method offers an incentive to the publisher of the ad to target the ad correctly. It will come up when certain keywords are used in visitors' searches that correspond with the content of the ad. Payment to the publisher is dependent upon viewers actually responding to the ad by clicking on the hyperlink within the ad.
- **Cost per Action (CPA)** The charge to the advertiser is based on the user completing a form, registering for a newsletter, or some other action that will lead to a sale. The publisher assumes all the risk in running this type of advertisement. Advertisers prefer this type of charge for banner advertisements.

DISADVANTAGES OF ONLINE ADVERTISING Many marketers have abused the Internet and its ease of use with excessive *spamming*—sending mass mailings by e-mail to Internet users. Excessive use of pop-ups, flashy banners, and spam has caused people to use pop-up blockers, spam control, and spyware to block promotions from reaching their computers.

Luisa creates a web site that provides information about her gourmet food shop and catering services. Because her customers are local, Luisa decides not to use any other forms of online advertising.

Television Advertising

Promotions on television reach millions of people every day. It is the best way to reach a large number of people quickly. Television advertising usually comes in the form of commercials and paid advertisements. Commercials are usually less than a minute in length and are run during breaks in television programming. They



Why do you think television advertising often targets teenagers?

are very short promotions about a product or business. Paid advertisements—also known as infomercials—can last a half hour or more and go into depth about the product being offered. Television promotion allows businesses to communicate through both sight and sound. It can be creative, entertaining, and informative.

Television advertising expenses include the fee you have to pay the station to air the commercial. This fee is based on the amount of time your advertisement or commercial plays. In addition, you must also consider the costs of producing the commercial. If a one-minute commercial costs \$25,000 to produce, you pay the television station \$2,000 for each minute it airs, and you plan to have it aired 30 times, the cost per minute would be $[\$25,000 + (\$2,000 \times 30)] \div 30 = \$2,833.33$.

DISADVANTAGES OF TELEVISION ADVERTISING Advertising on television is very expensive. Producing even a low-budget commercial can cost thousands of dollars. You will need to seek the help of video and production professionals when developing a television ad. In addition, you will have to pay a network or cable station to broadcast the commercial.

Television reaches too broad an audience to be effective for most businesses. If, for example, only one percent of the viewing audience is interested in a particular product, advertising on television is not likely to be cost-effective.

Because of the excessive costs and the fact that she may not reach her target customer very effectively, Luisa decides that television advertising is not right for her business.

Radio Advertising

Radio advertising can be effective for small businesses. It is less expensive than television promotion. You can also be more certain you are reaching your target market. Radio stations tend to attract a particular kind of listener. Pop rock stations target teenagers and people in their twenties. Classical or talk radio stations usually attract older listeners. Selecting a station whose listeners share the same demographics as your target market can increase the effectiveness of your advertising. You can contact stations and ask for a demographic profile of their listeners to make sure it fits your target market profile.

The costs of radio advertising are determined in the same way as the costs of television advertising. You must pay for air time and production costs.

DISADVANTAGES OF RADIO ADVERTISING

Radio is a purely audio message and can't visually show your product. Radio listeners may not remember what they hear. They

NETBookmark

In 1999, *Advertising Age* magazine recounted the history of the American advertising industry in the 20th century. Access school.cengage.com/entrepreneur/ideas and click on the link for Chapter 6. Read about some of the most famous and effective ad campaigns, jingles, slogans, and icons/spokespeople of the past 100 years. Then think about the current advertising slogans and spokespeople you see and hear every day. Do you believe any of them could be added to *Advertising Age*'s "best-of" lists? Explain why or why not.

school.cengage.com/entrepreneur/ideas

may tune out or even “surf the airwaves” during the commercial spots. You may need professional help when developing a radio ad, which can be costly.

Luisa is targeting middle-aged, upscale customers. To reach this audience, she decides to advertise on the classical music station in her community. She receives a demographic profile of the radio station’s listeners and determines that her business targets a similar type of person.

Newspaper Advertising

Newspapers have been the single largest form of advertising in the United States. However, as more people are looking to the Internet for news and information, newspaper circulation has dropped in many cities. Small businesses may choose to promote their products and services in the newspaper for the following reasons:

- It is relatively inexpensive.
- It targets a limited geographic area.
- It reaches large numbers of people.

Luisa decides to advertise in several local newspapers. She places quarter-page ads in the morning paper serving the citywide area. She also puts half-page ads in all of the free newspapers that serve her community. The community papers reach a much smaller audience than the large city newspaper, but they target the local audience Luisa is trying to reach. Advertising in newspapers represents a cost-effective way for Luisa to reach her target market.

DISADVANTAGES OF NEWSPAPER ADVERTISING Newspapers reach a large audience, but much of that audience may not be interested in your business. If, for example, you own a small gift shop that caters to people only in your immediate area, advertising in a large city newspaper with a wide circulation may not make sense. You would be paying to reach thousands of people who are outside of your target market.

Another disadvantage of newspaper advertising is the fact that your advertisement will compete with many others. Newspapers carry so many advertisements that readers may overlook yours.

Telephone Directory Advertising

Telephone directories list the phone numbers of people and businesses in a certain area. Directory ads usually appear on a page close to the listing and phone number of the business placing the ad. Directory ads can be similar in appearance to newspaper ads. Customers look in telephone directories again and again, making them a good advertising medium.

A disadvantage of directory advertising is that people look in the directory only when they are already in search of a particular type of business. With directory advertising, it is not easy to persuade customers to try your business instead of a competitor’s. But, knowing how important the phone book can be, Luisa decides to place a quarter-page ad in the commercial directory distributed in her area.



Direct-Mail Advertising

Direct-mail advertising includes fliers, catalogs, letters, and other correspondence sent to target customers through the mail. Mailing lists for target markets are available for purchase. If your business sells hospital beds, you can purchase targeted mailing lists of people who would purchase your product. You can also get lists of people based on the geographic area. Companies that specialize in maintaining targeted mailing lists can provide almost any kind of list for any kind of business.

Direct-mail advertising can be effective if people read it, but many people throw out direct-mail advertising, calling it “junk mail.” If you use this method of advertising, you will want to come up with an attention-grabbing design or other means of making people want to read it.

Luisa decides to use direct mail to target residents living in four ZIP code areas near her store. She creates an attractive brochure with a catchy slogan on the outside cover, and she mails it to residents in the neighborhoods she is targeting.

Magazine Advertising

Magazines are an excellent way to aim products and services at specific markets. Fitness magazines are full of advertisements for athletic apparel and equipment. Magazines targeting teenage girls are full of advertisements for products that appeal to them, such as cosmetics and clothing.

Most magazines are nationally distributed. This can make them inappropriate for businesses that sell in a limited geographic area. Some large cities have local magazines, which would be an effective way to target a certain area.



© Digital Vision

Why are magazines an effective advertising medium when you are trying to reach a specific target market?



The city in which Luisa will be opening her gourmet store has two local magazines. One focuses heavily on restaurants and entertaining. Luisa checks the demographics of the magazine's readership and finds that it targets the same market she is trying to reach. She decides to advertise in the magazine every other month.

Outdoor Advertising

Outdoor advertising includes billboards and signs. Such advertising can be effective in keeping the name of your business in a place where many people can see it. But because people view such advertising quickly as they drive by, it cannot include much information. Also, outdoor advertising may not project the image you are trying to convey for your business.



When do you think outdoor advertising is more effective than other forms of advertising?

Transit Advertising

Transit advertising consists of signs on public transportation. Transit advertising can provide more information than is typically seen on a billboard. Such advertising can be effective if the market you are trying to reach includes many people who use public transportation.

Luisa's target market lives in the suburbs and rarely uses public transportation. For this reason, she rules out transit advertising, which would not help her reach her target market.

Budgeting for Promotion

Once you determine your promotional mix, you must obtain the approximate costs for all forms of advertising media that you plan to use. Using the estimated costs, calculate a projected promotional budget. Compare this amount to your projected sales and decide what percentage of the budget promotion represents. Determine whether this budget is realistic for your business. Compare your percentage to the industry average, which you can obtain from trade associations, business publications, or business owners. Be sure your promotional budget is in line with similar businesses.

Checkpoint

Why is promotion important to a business?

Publicity

Publicity is a nonpaid form of communication that calls attention to your business through media coverage. Publicity may be good or bad. Good publicity can be as helpful as advertising. Publicity is free, but staging an event or bringing in a celebrity to generate publicity usually is not. While there are things you can do to attract positive media attention, publicity is largely out of a business's control.

Publicity can be negative if the media coverage is unfavorable. For example, some community newspapers publish listings of restaurants that have violated health code laws. Customers may see this publicity and stop eating at those restaurants.

Luisa plans to have an open house to mark her first day in business. She hopes that the media will do a story on her grand opening. To increase this chance, Luisa hires a popular local jazz band to perform. She also invites her community's leaders and personalities. She writes and sends a press release to all of the local newspapers, magazines, and radio and television stations as well. A **press release** is a written statement meant to inform the media of an event or product. Luisa's press release is shown on the next page.

To keep her name in the news, Luisa volunteers to write a weekly cooking column for one of the free newspapers in her community. She

WHAT WENT WRONG

Dental Promotion Leaves Bad Taste

Dr. George Nilsson, a periodontist, had built his practice by using dentist referrals and word-of-mouth promotions and by speaking at conferences. As a way to expand his business, he decided to develop a program for dentists that graphically tracked gum disease. It would take the guesswork out of whether or not a patient should go to a specialist. Dr. Nilsson designed a step-by-step program, including a video and printed guide. He started the PerioDent Company, investing \$150,000 in developing the program elements, another \$40,000 for initial inventory, and \$80,000 more for advertising and public relations.

PerioDent sent out mailings to dentists, periodontists, and schools. Dr. Nilsson took out full-page ads in professional journals. Unfortunately, after six months, sales were not as expected. There was a backlash of bad press from Dr. Nilsson's peers. The majority of

dentists resented the PerioDent program because they believed it questioned the way they had been diagnosing gum disease. Additionally, dentists accused it of having a negative impact on their income because it prompted some patients to visit periodontists instead of dentists. At the same time, some periodontists accused George of blatant self-promotion and greed.

Think Critically

1. What could have been done differently to advertise and promote the program?
2. How might publicity or public relations activities help improve PerioDent's image?



© Image Source

Plan your promotions carefully.

FOR IMMEDIATE RELEASE**GALA OPENING OF LUISA'S GOURMET LUXURIES**

Come celebrate the opening of Luisa's Gourmet Luxuries on Friday, September 20, at 8:00 P.M. Hors d'oeuvres, imported champagne, and French pastries will be served at the event. Music will be provided by Glendale's leading jazz ensemble, Jazz Expressions.

The opening of Luisa's Gourmet Luxuries marks the realization of a dream by owner Luisa Ramirez. "As a specialty cook," she says, "I could not always find the products I needed. And I was never happy with the selection of produce and baked goods in town." Luisa decided to open a store that would offer the kinds of products she could not find elsewhere in town.

Luisa's Gourmet Luxuries offers an astounding selection of products, including 14 different kinds of olive oil, 12 different kinds of rice, and pasta products from several different countries. "Everyone's taste is different," says Luisa, "so I offer a large selection."

For more information contact:

Luisa Ramirez, Proprietor

Luisa's Gourmet Luxuries

1610 Marbury Road, Glendale, CT

(275) 555-3983

likes the opportunity to educate the public about gourmet cooking and to increase her store's visibility as a seller of gourmet foods.

Public Relations

Public relations is the act of establishing a favorable relationship with customers and the general public. Public awareness and positive public relations can be generated for your business when you show your community that you are involved and committed to it. There are many ways to support your community, including the following:

- Sponsor a community sports team.
- Make a donation to a local charity or relief effort program.
- Get involved with the work-based program at your local high school or community college.
- Become active in the local chapters of the Big Brothers or Big Sisters organizations.
- Organize community programs such as cleaning up neighborhood parks.



Self-Promotion

A business should try to keep its name visible and in the forefront of people's minds. Self-promotion is a good way to do this. It's a simple way to generate "free" publicity. Self-promotion may include activities such as the following:

- Giving away t-shirts and hats displaying your company name and logo.
- Distributing pens, notepads, coffee mugs, and other useful items printed with the name, telephone number, web site address, and logo of your business.

Checkpoint

What are the advantages and disadvantages of publicity?

6.2 Assessment

THINK ABOUT IT

1. Why is it important for a business to consider its target market when selecting an advertising medium?
2. Describe some public relations activities businesses in your area have performed.
3. How would you decide which method of advertising is the best and most cost-effective for your business?

MAKE ACADEMIC CONNECTIONS

4. **PROBLEM SOLVING** You are opening a new gardening service business in your community. You will help your customers plan their flower and vegetable gardens and shop for the plants for them. You will also provide planting services if your customers need them. Use the six-step problem-solving method to determine how to advertise the grand opening of your business.
5. **MATH** You have produced a one-minute television commercial for \$20,000. You plan to air it on a local television station for a cost of \$1,000 per minute. You plan to air the commercial 20 times. What is the advertising cost per minute?



TEAMWORK

Working with team members, plan the grand opening activities for Fit For U, a fitness center that provides personal trainers for all clients along with a personalized fitness plan. Describe all of the promotional activities that you will conduct for the business. Write a press release to inform the local media of the opening.



6.3

Selling and Promoting

Goals

- Explain the role of selling in a business.
- Determine how to meet customer needs and wants.
- Discuss other types of promotional activities.

Terms

- personal selling
- rational buying decisions
- emotional buying decisions
- sales promotion
- rebate
- telemarketing

Focus on Small Business

Expanding the business

JoJo started her dance studio five years ago. Over the years, many of her clients have expressed a desire for JoJo to sell dance attire and shoes at her studio. She looks into the idea of adding a clothing line and thinks that it would be a good addition to her business. She decides to hire Claire to run the clothing side of the business. Claire has worked in retail sales for over ten years and is very customer-oriented. By adding Claire to her staff, JoJo will be able to offer her clients another service to meet their needs. In addition to her dance clients, JoJo wants to make the clothing line available to the general public.

Work as a Team Do you think that JoJo is making a good decision in adding a retail clothing line to her dance studio? Why or why not? What kinds of promotions do you think JoJo should use to try to attract new customers?



© Getty Images/PhotoDisc

Businesses must create the right promotional mix to attract customers.

Selling

Good selling skills are important to an entrepreneur. You will be selling your business ideas to potential investors in the beginning stages of developing your business, and you will be selling products or services to customers once you open your business. You might need to hire others to assist you with your business, and you will need to be sure that they also have good selling skills.

To many customers, the salesperson is the business. This may be the only representative of the company the customers ever come in contact with, so it is important for the salesperson to create a positive image of the company. Selling is the way a business makes money, so a salesperson plays a very important role.



© Getty Images/PhotoDisc

Why do you think personal selling is an important component in the success of retail stores, such as hardware stores?

Personal Selling

Personal selling is direct communication between a prospective buyer and a sales representative in which the sales representative attempts to influence the prospective buyer in a purchase situation. It is important for the salesperson to uncover and identify the customer's needs, issues, and concerns so that they can be addressed throughout the sales process.

Product Knowledge

To be successful at selling a product or service, a salesperson must have thorough knowledge of the features and benefits of the product or service. *Features* are the physical characteristics or capabilities of the product or service. *Benefits* are the advantages that could result from those features. Customers are mainly interested in the benefits they will receive from purchasing a product or service. Many times a salesperson builds a sales presentation around the features alone. However, customers who see the benefits of purchasing the product or service will be less likely to object to the price of the item as the sales transaction progresses.

It is important for a business to spend time training salespeople about the product or service being sold as well as the industry in which they are working and the market in which they are selling. They should also be familiar with their own company as well as their company's competition. The more salespeople know about the internal and external environment in which they are working, the more effective they will be.

Checkpoint

Why is selling important to a business?



Determine Customer Needs and Wants

Customers purchase goods and services in order to satisfy needs. The need may be as basic as food, water, or shelter. Or, it may be a more complex need, like the need for esteem. A salesperson must determine what need the customer is seeking to satisfy in order to sell a product or service to meet the need. Lower-level needs are not usually met through personal selling. Customers *must* purchase certain items to satisfy their basic needs and do not need the assistance of a salesperson. Selling skills become more important as customers are seeking to meet upper-level needs.

Needs Assessment

Customer needs within a target market can be identified through marketing research. The information helps a business decide what type of product or service to offer customers. When an individual customer goes shopping, it is up to the salesperson to find out as much as possible about the customer's situation by conducting a needs assessment. This involves interviewing the customer to determine his or her specific needs and wants. The salesperson can then help identify the range of options the customer has for satisfying those needs and wants.

Some customers will know exactly what they want, and the fulfillment of their needs is referred to as *need satisfying*. Even though the customer knows what he or she wants, the salesperson must be flexible and willing to commit company resources and selling time in order to better satisfy needs. When the need is not identified, the process of satisfying the need is called *problem resolution*. Problem resolution requires the salesperson to adopt the customer's point of view, ask questions to assess the nature of needs and specific requirements, and act as a consultant to assist the customer in solving the problem.

Buying Decisions

Customers are influenced by rational and emotional buying motives. **Rational buying decisions** are based on the logical reasoning of customers. Customers evaluate their options and make a purchase only after careful thought. Rational buying motives include safety, simplicity, quality, reliability, economy, convenience, service, durability, knowledge, money gain, and ease of operation. **Emotional buying decisions** are based on the desire to have a specific product or service. Feelings, beliefs, and attitudes can influence buying decisions. Often, little thought or time is spent making an emotional decision. Some emotional buying motives include fear, protection, appearance, recreation, improved health, comfort, recognition, pride of ownership, imitation, prestige, and popularity.

Customer Decision-Making Process

Following a problem-solving process is the best way to make a decision. This is also true with customers when they are making a decision to purchase a product or service. The steps are to define the problem, gather information, identify various solutions, evaluate alternatives and



select the best option, take action, and evaluate the action. A salesperson can assist customers through this process by helping them define their need, showing them all the products or services that could meet the need, explaining the features and benefits of the various options, making the sale, and following up with the customer.

Checkpoint

Why is it important to meet customer needs and wants in the selling process?

Other Types of Promotion

Advertising, publicity, and personal selling are not the only ways to draw attention to your business. You can also offer sales promotions or use telemarketing to promote your business.

Famous Entrepreneur

Anne Barge

Playing with paper dolls as a child led Anne Barge to her multimillion-dollar business selling bridal gowns. Internationally known as an expert in the field of bridal wear, her designs are rooted in research and inspired by vintage culture. Anne is involved in the development of each gown bearing her name and offers three distinctive brands that can satisfy any customer's taste and budget. Customer service is her top concern, and she helps each customer have a unique style for her special day.

Anne began her career in the fashion field by working for others. In 1996, Richard Branson, owner of Virgin Records music label, asked Anne to set up a bridal store in London for him. As manager of Virgin Bride, she introduced British brides to a totally new look. Even the British tradition of having only children as attendants changed when Anne introduced adult

bridesmaid gowns to the United Kingdom.

In 1999, Anne decided to become an entrepreneur. She opened a bridal store in Atlanta, Georgia, and launched the Anne Barge Bridal Collection. Her collection combined classic designs in the finest of silks with museum-quality beading and embroidery, never seen before in the worldwide bridal market. Now her line is represented in over 100 of the finest stores in the United States, the United Kingdom, Spain, and Japan. The designing dreams of a little girl have come true in a big way!

Think Critically

How important is Anne's commitment to customer service to the success of her business? Why do you think brides would choose one of Anne's gowns over those of another designer?



© Chris Nicholls

Do you think working for others before becoming an entrepreneur contributed to Anne's success?

A **sales promotion** is an incentive offered to customers in order to increase sales. Examples of sales promotions include:

- contests
- free samples
- rebates
- coupons
- special events
- gift certificates
- frequent-buyer reward programs

Some companies offer rebates. A **rebate** is a refund offered to people who purchase a product. Customers who purchase a \$12 bottle of olive oil may be entitled to a \$2 rebate from the manufacturer.

Telemarketing is using the phone to market your product or service. It can be an inexpensive, effective way to let people know about your business or about special offers. Keep in mind that some consumers consider telemarketing to be annoying and would rather not be contacted while they are relaxing at home.

Checkpoint

What is the purpose of sales promotions?

6.3 Assessment

THINK ABOUT IT

1. Why is personal selling used in a business?
2. What is the purpose of the needs assessment?
3. Name some sales promotions that an entrepreneur might use. Can you think of examples in addition to the ones listed in the lesson?

MAKE ACADEMIC CONNECTIONS



4. **MARKETING** Customers are more likely to purchase a product if they clearly see its benefits. When selling products, you must learn to sell product benefits rather than product features. Using the Activity CD, open the activity, "Turn Features into Benefits." Print a copy and complete the activity.
5. **COMMUNICATION** You plan to use telemarketing to market your pressure-washing business to people in your local community. You can wash driveways, walkways, patios, decks, vinyl siding, and lawn furniture. Write a script you will use when making the sales calls.



TEAMWORK

Working in a team, choose a business in your community. Make a list of all the marketing efforts that this business uses. Outline what you think the marketing plan for this business would look like.



Sharpen Your Entrepreneurial Skills

Marketing and the Web

Many people believe that using the Internet for marketing a business is essential to its success. There are many electronic tools available, and you will need to analyze them to be sure you are using the right tools for your business. As an entrepreneur, it will be up to you to evaluate the best way to use the Web to market your business.

Some of the advantages of using Web technology include:

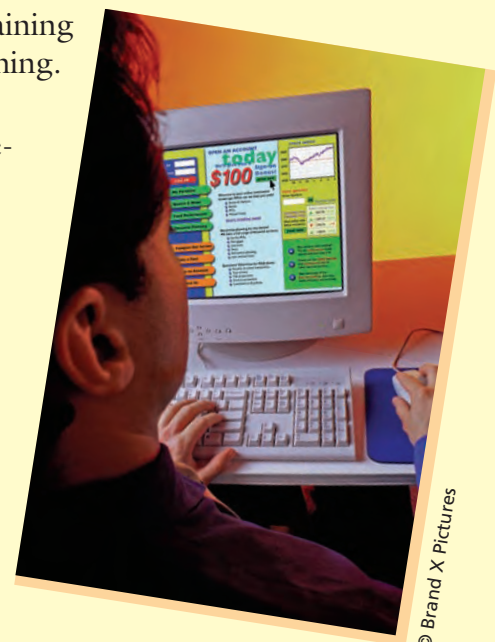
- **Cost savings** It is much cheaper to send an e-mail with marketing information than it is to print and mail advertisements.
- **New customers** A web site can attract new customers from all over the world to your business.
- **Networking Opportunities** You can use blogs, message boards, and online discussion groups to network with many people.

Some of the disadvantages of Web technology include:

- **Ineffective e-mails** If someone does not already know about your business, e-mail might not be the best way to reach him or her. Many people delete mail from senders they do not know and use spam filters to keep such mail from reaching their inbox.
- **Loss of personal contact** You lose the personal contact with your customers if you rely only on the Web to communicate with them. Many people hesitate to do business with someone that they have not met.
- **Expense of maintaining web site** Developing and maintaining an effective web site can be very expensive and time-consuming.
- **Inefficient use of time** Responding to numerous general inquiries from people using your web site can be very time-consuming. It would be more efficient to have a FAQs (Frequently Asked Questions) page on your web site that provides answers to commonly asked questions.

TRY IT OUT

You own a print shop that prints fliers, business cards, catalogs, and stationery for local businesses. You are considering creating a web site for your business. Make a list of purposes for which you might use the site. Then determine the advantages and disadvantages of using the web site for the purposes you listed. Evaluate whether the Web could be a valuable marketing tool for your business.



© Brand X Pictures

Chapter 6 | Assessment

SUMMARY

6.1 The Marketing Mix—Distribution

1. The four basic options for channels of distribution are: (1) manufacturer to consumer; (2) manufacturer to retailer to consumer; (3) manufacturer to wholesaler to retailer to consumer; and (4) manufacturer to agent to wholesaler to retailer to consumer.
2. Entrepreneurs should examine the different options for channels of distribution and choose the one that best meets the needs of their business and their customers.
3. Transportation, product storage and handling, and packaging needs are all factors that play an important role when choosing methods of physical distribution.

6.2 The Marketing Mix—Promotion

4. Advertising may be done on the Internet, on television, on radio, in the newspaper, in a telephone directory, through direct mailings, in magazines, and on billboards and signs. Each advertising medium has its own set of advantages and disadvantages. The best option for a business is the one that reaches the desired target market in the most cost-effective way.
5. Publicity is a nonpaid form of communication that calls attention to your business through media coverage. A business may capture media attention by submitting a press release and through public relations activities.

6.3 Selling and Promoting

6. Selling skills are important because sales are how a business makes money. A salesperson must identify the customer's needs, issues, and concerns so that they can be addressed throughout the sales process. To be successful, a salesperson must have a thorough knowledge of the features and benefits of the product or service.
7. Needs assessment involves interviewing the customer to determine the customer's specific needs and wants. Customers' buying decisions may be rational (based on logic) or emotional (based on desire). Customers often use the problem-solving process to make buying decisions. The salesperson can assist customers during each step of this process.
8. Offering an incentive to customers in order to increase sales is called sales promotion. Examples include contests, frequent-buyer reward programs, rebates, free samples, special events, coupons, and gifts. Telemarketing is an effective way to let people know about your business and special offers.

What do you know now?

Read Ideas in Action on page 147 again. Then answer the questions a second time. How have your responses changed?

VOCABULARY BUILDER

Match each statement with the term that best defines it. Some terms may not be used.

1. Routes that products and services take from the time they are produced to the time they are consumed
2. Moves the product directly from the manufacturer to the consumer
3. Uses intermediaries that move products between the manufacturer and the consumer
4. A paid form of communication sent out by a business about a product or service
5. The act of establishing a favorable relationship with customers and the general public
6. Direct communication between a prospective buyer and a sales representative
7. Purchase decisions based on the logical reasoning of customers
8. An incentive offered to customers in order to increase sales
9. A nonpaid form of communication that calls attention to your business through media coverage
10. A written statement meant to inform the media of an event or product
11. Purchase decisions based on the desire to have a specific product or service
12. A refund offered to people who purchase a product

- a. advertising
- b. channels of distribution
- c. direct channel
- d. distribution
- e. emotional buying decisions
- f. indirect channel
- g. personal selling
- h. physical distribution
- i. press release
- j. public relations
- k. publicity
- l. rational buying decisions
- m. rebate
- n. sales promotion
- o. telemarketing

REVIEW YOUR KNOWLEDGE

13. Which of the following type of business is least likely to distribute its products or services directly to consumers?
 - a. retail business
 - b. service business
 - c. manufacturing business
 - d. none of the above directly distribute products to consumers
14. Which channel of distribution would be best for someone who makes and sells pottery at his or her home?
 - a. manufacturer to consumer
 - b. manufacturer to retailer to consumer
 - c. manufacturer to wholesaler to retailer to consumer
 - d. manufacturer to agent to wholesaler to retailer to consumer
15. True or False: Agents and wholesalers are intermediaries that facilitate the flow of goods through direct channels of distribution.
16. Goods that arrive at their destination damaged probably have a problem with the _?_ in the physical distribution process.
17. Examples of promotion include

a. advertising	c. sales promotion
b. publicity	d. all of the above
18. **True or False?** Publicity is always good for a business.

19. If you have a local business that offers a service to consumers in your neighborhood, which of the following would be the best way for you to advertise?
 - a. a commercial aired during the Super Bowl
 - b. an advertisement on satellite radio
 - c. an advertisement in the local newspaper
 - d. a billboard on a major interstate highway
20. An online ad that changes the background of the page being viewed is a
 - a. banner ad
 - b. floating ad
 - c. wallpaper ad
 - d. trick banner
21. Which of the following is the least important in the sales process?
 - a. customer's needs
 - b. customer's issues
 - c. customer's concerns
 - d. customer's income
22. Which of the following would be the best way for you to promote your pressure-washing business?
 - a. free sample
 - b. discount coupon
 - c. contest
 - d. gift with purchase
23. A salesperson who approaches all customers the same way is leaving out which important part of the sales process?
 - a. needs assessment
 - b. product knowledge
 - c. rational buying decisions
 - d. none of the above

APPLY WHAT YOU LEARNED

24. You are a home improvement contractor. What role will channels of distribution play in your business? Which form of promotion will work best for you? Why? How can you assist your customers in their decision-making process?
25. You are going to open a retail store that will offer gifts and accessories. Your target market is 13- to 15-year-old girls. Describe the promotional mix you will use for your business.

MAKE ACADEMIC CONNECTIONS



26. **MARKETING** When creating advertisements and promotions for your products, you must know who your target market is in order to create a message that will be effective. Using the Activity CD, open the activity, "Who Is the Target Audience?" Print a copy and complete the activity.
27. **COMMUNICATION** You are opening a health club and spa. Write a press release to local newspapers and radio and television stations. You are also buying time on a local radio station. Write the commercial that will air on the radio. List some public relations activities that could promote your business.
28. **RESEARCH** Many companies have reward programs for their customers. Research the reward program of a company with which you are familiar. Prepare a presentation about the program, including information on who is eligible, how customers participate, and the rewards available to participants. How does the reward program help build customer loyalty? Present your findings to the class.

29. **MATH** You have placed an ad on the Internet that is going to be charged using the CPA method at a rate of 50 cents per registered visitor. During one week, your web site received 75,345 hits from visitors linking from the advertisement, 12,000 of those inquired about your product, and 7,432 of them registered their personal information with your web site. How much will you have to pay the publisher of your ad?

WHAT WOULD YOU DO?



You are the owner of Cookies For You. You have been selling your cookies in gift baskets designed for adults. Recently, you decided to start offering cookie gift baskets for children as well. You are thinking about doing a promotional activity at a local day-care center in which you will give free cookies to all of the children. However, with all of the recent news reports and stories about childhood obesity, you are not sure that you should be promoting cookies to children. You are concerned that your marketing strategy will be viewed negatively.

What would you do? Is it your responsibility to monitor the eating habits of children, or is this something for which only their parents should be responsible? How can you promote your cookie gift baskets in a positive way?

BUILD YOUR Business Plan *Project*

This activity will help you complete the marketing plan for your business idea.

1. Determine the channels of distribution that you will use for your business. Include information on how you will get products from your suppliers as well as how you will distribute your products or services to your customers.
2. Develop selling strategies and company policies to ensure that the internal environment of your business promotes good customer relations.
3. Get advertising rates for a local radio station, television station, and newspaper. Also obtain rates for Internet advertising. Choose the medium that is best for your business and write an advertisement for that medium.
4. To generate publicity, write a press release that you will send to the media.
5. After you have completed your marketing plan, review it to be sure that the questions listed on page 124 in Chapter 5 are answered. If necessary, revise your marketing plan as needed to ensure that all of these questions are addressed.

Planning a Career in Public Safety



"My dad's girlfriend is excited about starting a business with her new partner. Although she likes her prospective partner, she has hired a reputable private investigator to do a complete background check. She wants to be sure there's nothing in this person's background that could impede the progress of their business."

How do individuals check the backgrounds of household employees? How do corporations, within the confines of the law, determine their employees are honest?

Private investigators provide a variety of services to individuals and corporations including child support investigations, employee background checks, and corporate asset protection.

EMPLOYMENT OUTLOOK

- Faster than average job growth is expected.
- The need to protect confidential and proprietary information will drive an ongoing need for private investigators.
- About one-quarter of private investigators are self-employed.

JOB TITLES

- Insurance Fraud Investigator
- Surveillance Operative
- Assets Protection Investigator
- Loss Prevention Detective
- Certified Legal Investigator
- Hotel Detective

NEEDED SKILLS

- Many private investigators are retired military or law enforcement professionals.
- Investigators often have prior work experience in fields related

to their investigative area of expertise.

- A degree in criminal justice can be helpful.
- Most states require licensing.

What's it like to work in Public Safety

Otto, a self-employed private investigator, has spent the early part of his day performing hidden surveillance. His client, an industrial manufacturing firm, suspected fraudulent filing of a workers' compensation claim by an employee. The employee claimed that a recurring on-the-job back injury prohibited her from reporting to work. Otto had just finished his final surveillance of the employee. Today, she was playing tennis at a local park. Otto now had photos and video coverage of the employee in multiple scenarios performing physical activities that a back injury would prevent. Otto's client will be able to prove fraudulent filing of workers' compensation claims.

Otto is looking forward to dinner this evening as the client is buying! The client, who is the owner of a local restaurant chain, hired Otto to investigate potential employee theft. Otto has been collecting data through hidden video cameras. Tonight, as he dines at the restaurant, he will focus his observation on one of the servers who is suspected of undercharging friends and family for their meals.

What about you? Would you enjoy lawfully tracking down information that could help individuals and companies do a better job of protecting their rights?



ENTREPRENEURSHIP PROMOTION PROJECT

The Entrepreneurship Promotion Project provides students an opportunity to demonstrate the skills needed in planning, organizing, implementing, and evaluating a campaign to educate chapter members and other individuals about entrepreneurship opportunities. Chapter members will utilize their knowledge of entrepreneurship and marketing skills to communicate the benefits of entrepreneurship to the target audience. Participants will share the information with a selected audience in the community (examples: middle-school students, elementary students, civic organizations).

This project can be completed by one to three students. It includes a written plan and oral presentation. Major sections in the body of the written plan include the Executive Summary; Introduction; Management of Activities to Inform Chapter Members; Management of Activities Targeted at Outside Audience; Evaluation and Recommendations; Bibliography; and Appendix (optional).

PERFORMANCE INDICATORS EVALUATED

- Demonstrate knowledge and understanding of entrepreneurship.
- Engage in activities that clarify and enhance understanding of entrepreneurship.
- Plan and implement presentation/activities to educate and promote entrepreneurship to targeted groups.
- Derive facts from data, findings from facts, conclusions from findings, and recommendations from conclusions.
- Demonstrate critical-thinking skills.
- Develop a concept from an idea to reality.
- Plan, organize, and conduct a group project.
- Determine priorities and set deadlines.
- Evaluate group presentations.

Go to the DECA web site for more detailed information.

Think Critically

1. What are the benefits of presenting this project to elementary or middle-school students?
2. Why is it important to explain risks involved with entrepreneurship?
3. Who are popular examples of entrepreneurs?
4. What are three characteristics of successful entrepreneurs?

www.deca.org

Chapter 7



Select a Type of Ownership

7.1 Decide to Purchase, Join, or Start a Business

7.2 Choose a Legal Form of Business

7.3 Legal Issues and Business Ownership

school.cengage.com/entrepreneur/ideas

IDEAS IN ACTION

Capitalize on Youth Marketing

The corporations of today were started as small businesses—often with single owners—at some time in the past. Such is the case with The Buzz International Marketing Group, Inc. Tina Wells started The Buzz, her first business, when she was just 16-years old. Ten years later, she found herself named as one of *Entrepreneur* magazine's "Young Millionaires" and the CEO of The Buzz Marketing Group, Inc.

Tina has been able to build a career doing what she loves. She always had a love for fashion and a fascination with pop culture. At 16, she began writing reviews for *New Girl Times*, a newspaper for young girls, of companies and their products that targeted teens. For her work, she received free products from more than 40 companies. After three months, she called on ten of her friends to help her, and they started The Buzz. Tina noticed that companies were not really connecting with the teens they were targeting as customers, so she began submitting her reviews directly to the companies. She was amazed by the positive response she received from the companies. A marketing director at one company told her that she had just paid someone \$25,000 for the same type of information, but that Tina's report was better! This was when Tina realized she could get paid for doing what she loved. And so, the Buzz Marketing Group was born. She got her first paying client while she was a freshman in college.

Tina went on to earn her B.A. in Communication Arts from Hood College. She felt that her degree gave her more credibility as a businesswoman. Today the Buzz International Marketing Group, Inc. is headquartered in New York City and employs ten people. In addition to the staff, over 9,000 teenage and young adult "buzzspotters" are out researching what their peers are thinking and doing. The buzzspotters help Tina stay in touch with what's happening.

Tina realizes that the profits from her business must be reinvested in the business in order to keep it growing. Even though she loves to shop, she invests profits into training seminars for the "buzzspotters" and other things that will contribute to the success of her business.

Today Tina speaks regularly to professional audiences across the country. She has been quoted and featured in numerous business publications, including *O Magazine*, *New York Times*, *Ebony*, and *Entrepreneur*.



© Matthew Peyton/Getty Images

Tina Wells, CEO of The Buzz Marketing Group, Inc.

What do you know?

1. What unmet need did Tina find that led to her first business?
2. Tina set up her business as a corporation. What is a corporation?
3. Name some of today's successful corporations that started out as a small business owned by one or two people.

7.1

Decide to Purchase, Join, or Start a Business

Goals

- Discuss purchasing an existing business.
- Describe how to evaluate a franchise opportunity.
- List advantages and disadvantages of joining a family business.
- Determine whether to start a new business.

Terms

- franchise
- initial franchise fee
- startup costs
- royalty fees
- advertising fees

Focus on Small Business

How can we get this dough rising?

After graduating from the culinary arts institute, Midori and Crystal wanted to realize their dream of owning a bakery. Midori found an ad for a bakery that was for sale. "If we purchased it, we would have the equipment and supplies needed to get started right away," she told Crystal. "If that's the Holcombe family bakery, we'd better stay away," Crystal warned Midori. "I was in there last week, and Mrs. Holcombe and her daughter were fighting about something. No one was waiting on the customers, and everyone was getting upset. If we bought that bakery, we would have to do something to change people's opinions about the service."

"We could always start our own bakery 'from scratch,'" Crystal suggested. "Very funny!" Midori replied. "But that could be hard too. We would have to find a location, buy everything we need, and build a customer base." "Well," Crystal said, "maybe we should buy a franchise." "That's a possibility, but we'd have to follow the rules and regulations set by the franchise company," Midori said. "Gosh, it's not easy to get the dough rising, is it?" Crystal replied.

Work as a Team What do you think would be some of the advantages and disadvantages to Midori and Crystal of starting a business from scratch, buying an existing business, or buying a franchise?



© Getty Images/PhotoDisc

There are many ways to begin a business venture.

Purchase an Existing Business

When most people consider going into business for themselves, they think about starting a new business. But purchasing an existing business could be a good option. Owners sell their businesses for a variety of reasons. Reasons can include insufficient sales or profits, new competition, fear of changing economic conditions, retirement, a dispute among partners, death or illness of a partner, and the owner's desire to do something different.

There are many ways to find businesses that are for sale. You may find advertisements in the classified section of the local newspaper. You might decide to use a business broker who sells businesses for a living. Other people in your industry might know of businesses for sale. You might also learn about available businesses through landlords and leasing agents, lawyers and bankers, management consultants, the Small Business Administration, the Chamber of Commerce, and bankruptcy announcements.

Advantages of Buying an Existing Business

There are many advantages to buying an existing business.

1. **The existing business already has the necessary equipment, suppliers, and procedures in place.** It may also have built up *goodwill*, or customer loyalty. You may want to change some of the policies and procedures established by the former owner, but fine-tuning existing systems is likely to be much easier than creating systems from scratch.
2. **The seller of a business may train a new owner.** The previous owner or experienced employees may be willing to help the new owner learn about the company.
3. **There are prior records of revenues, expenses, and profits.** This means that financial planning will be easier and more reliable than it would be for a completely new business.
4. **Financial arrangements can be easier.** The seller of the business may accept an initial partial payment and allow the rest to be paid off in monthly installments. This can reduce or eliminate the need for bank financing. If bank financing is needed, getting it may be easier because banks are more likely to lend to an established business.

Disadvantages of Buying an Existing Business

Buying an existing business sounds like an easy way to become an entrepreneur, but it can be risky. There are disadvantages to buying a business.

1. **Many businesses are for sale because they are not making a profit.** Owners often try to sell businesses that are not financially profitable.
2. **Serious problems may be inherited.** Businesses can have poor reputations with customers, have trouble with suppliers, or be poorly located.
3. **Capital is required.** Many new entrepreneurs just do not have the money to purchase a mature business. Starting small may be their only option.

Steps in Purchasing a Business

Buying a business is a complicated process that requires serious thought. If you are considering buying a business, you will want to follow these steps:

1. **Write specific objectives about the kind of business you want to buy, and identify businesses for sale that meet your objectives.** This will help you find the right business for what you want to do.

★ Develop Your Reading Skills

Before reading the chapter, make a list of questions you have about the different types of business ownership and the legal issues facing business owners. Try to find answers to your questions as you read the chapter.



2. **Meet with business sellers or brokers to investigate specific opportunities.** Ask about the history of the business, the reason for its sale, its financial performance, and the price the owner is asking for it.
3. **Visit during business hours to observe the business in action.** Inspect the facility closely to make sure that it meets your needs. Observe how the business operates when it is open to customers.
4. **Ask the owner to provide you with a complete financial accounting of operations for at least the past three years.** Analyzing these reports will help you see how much profit you can make and how much you will probably be paying out in expenses.
5. **Ask for important information in written form.** Get a list of all assets to be transferred to the new owner, a statement about any past or pending legal action against the business, a copy of the business lease or mortgage, and a list of all the suppliers. Have an accountant and a lawyer help you review all of the material. Be suspicious if the owner refuses to provide all of the information you request.
6. **Determine how you would finance the business.** Contact lending institutions, and ask the seller if he or she would be willing to finance part or all of the purchase.
7. **Get expert help to determine a price to offer for the business.** An accountant or a *valuator*—an expert on determining the value of a business—can help. Present the offer in writing to the seller. If an agreement is reached, have a lawyer draw up a sales contract.

Checkpoint

What are some of the advantages and disadvantages of buying an existing business?

Franchise Ownership

Purchasing a franchise is another route by which you can become an entrepreneur. A **franchise** is a legal agreement that gives an individual the right to market a company's products or services in a particular area. A *franchisee* is the person who purchases a franchise agreement. A *franchisor* is the person or company that offers a franchise for purchase.

More than 770,000 people in the United States own franchises, and the number is growing. Franchising opportunities are available in virtually every field, from motels to pet stores to video outlets. *The Franchise Opportunities Handbook*, a publication of the U.S. Department of Commerce, lists more than 1,400 franchise opportunities by category. It also provides information about the costs and capital requirements. Additional sources for finding out about franchise opportunities include the following:

- *A Consumer Guide to Buying a Franchise*, published by the Federal Trade Commission
- Books on franchising available at your public library



- *The Wall Street Journal*
- Magazines such as *Forbes*, *Barron's*, *Business Start-Ups*, *Entrepreneur*, and *Inc*

Operating Costs of a Franchise

If you decide to purchase a franchise, you will have to pay an initial franchise fee, startup costs, royalty fees, and advertising fees. The **initial franchise fee** is the amount the local franchise owner pays in return for the right to run the franchise. The fee can run anywhere from a few thousand to a few hundred thousand dollars. It is usually nonrefundable. **Startup costs** are the costs associated with beginning a business. They include the costs of renting a facility, equipping the outlet, and purchasing inventory. **Royalty fees** are weekly or monthly payments made by the local owner to the franchise company. These payments usually are a percentage of your franchise's income.

Advertising fees are paid to the franchise company to support television, magazine, or other advertising of the franchise as a whole.

Jim Saurbrey purchased a Subway restaurant franchise. For the right to use the Subway name and logo, Jim paid a franchise fee of \$12,500. In addition, Jim spent \$70,000 renting restaurant space, purchasing equipment and supplies, and obtaining legal and accounting services. During its first year, Jim's franchise earned \$36,000 in profits. He paid 8 percent, or \$2,880, to Subway in royalty fees. During Jim's second year in business, his restaurant earned \$51,000, and he paid \$4,080 in royalty fees.

Investigate the Franchise Opportunity

The Federal Trade Commission's (FTC) Franchise and Business Opportunity Rule requires franchise and business opportunity sellers to give you specific information to help you make an informed decision about your purchase. The seller must give you a detailed disclosure document at least ten business days before you pay any money or legally commit yourself to a purchase. You can use these disclosures to help answer your questions about the franchise or to compare it with other opportunities you are considering. The disclosure document should include the following:

- Names, addresses, and telephone numbers of at least ten previous purchasers who live nearest to you
- The fully audited financial statements of the seller
- Background and experience of the business's key executives
- Cost of starting and maintaining the business
- The responsibilities you and the seller will have once you have invested in the opportunity

If the seller does not give you a disclosure document, you should ask why. Then verify the explanation with an attorney, a business advisor, or the FTC.



Why do you think cleaning service franchises are so popular?



Evaluate a Franchise

Some of the things you should do when evaluating a franchise include the following:

1. **Study the disclosure document and proposed contract carefully.** Make sure all of the information listed above is included in the disclosure document. All costs and royalty fees should be provided.
2. **Interview current owners listed in the disclosure document carefully.** Ask them if the information in the disclosure document matches their experiences with the company. Be aware of *shills*, people listed in the document that are paid to give favorable reports.
3. **Investigate the franchisor's history and profitability.** Determine how long the franchisor has been in business and review its financial performance.



© Getty Images/PhotoDisc

Why is it important to research a franchise before you buy it?

4. **Investigate claims about your potential earnings.** The company should provide you with the written basis for any claims made about potential earnings. Determine the projected demand for the franchised product or service in the area where you will locate. Does the demand match the potential earnings?
5. **Obtain from sellers in writing the number and percentage of owners who have done as well as they claim you will.** Sellers are required by law to provide this information.
6. **Listen carefully to sales presentations.** Be cautious of any sales presentation that pressures you to sign up immediately. A seller with a good offer does not use high-pressure sales tactics. Don't fall for a promise of *easy money*. Remember that success usually requires hard work.

7. **Shop around.** Compare franchises with other business opportunities. Different companies offer different benefits. Choose franchises that interest you and request disclosure documents. Find out what services the franchisor offers. For example, will the franchisor help with marketing, merchandising, and site selection?
8. **Get the seller's promises in writing.** All promises made should be included in the written contract that you sign. Remember, the contract is a legally binding document.
9. **Determine what will happen if you want to cancel the franchise agreement.** Buying a franchise is a major investment, so you should determine the financial risks of canceling the franchise agreement.
10. **Remember that it is okay to ask for advice from professionals.** Lawyers, accountants, or business advisors can review the disclosure document and contract and give you their professional opinions about them. The money you spend for this service could save you from making a bad decision about investing in the franchise.



Advantages of Owning a Franchise

When deciding whether to buy a franchise, you should also consider the advantages and disadvantages of it. There are four main advantages.

1. **An entrepreneur is provided with an established product or service.** This allows entrepreneurs to compete with large, well-known companies.
2. **Franchisors offer management, technical, and other assistance.** This may include onsite training or classes, aid with starting the new business and handling daily operations, and tips on crisis management. Some franchisors even offer help on everything from site selection and building design to equipment purchase and recipes. Most also maintain toll-free telephone numbers that franchisees can call for advice.
3. **Equipment and supplies can be less expensive.** A large franchise may be able to purchase in huge quantities. Some of the savings they enjoy as bulk purchasers are passed on to the franchisee.
4. **A guarantee of consistency attracts customers.** A franchise contract mandates a certain level of quality. Consumers know that they can walk into a franchise anywhere in the country and receive the same product or service. The cheeseburger sold at a Wendy's in Long Beach, California, will be very similar to the cheeseburger sold in Toledo, Ohio.

Disadvantages of Owning a Franchise

Although franchising sounds like a great idea, there are some disadvantages that you need to consider.

1. **Franchise fees can be costly and cut down on profits.** The initial capital needed to purchase a franchise business often is high. Also, some of the profits you earn as a franchise owner are returned to the franchisor as royalty fees.
2. **Owners of franchises have less freedom to make decisions than other entrepreneurs.** Many business decisions that entrepreneurs generally make themselves have already been made for franchisees. Franchisees must offer only certain products or services, and they must charge prices set by the franchisor. Many entrepreneurs object to this control because it inhibits the freedom they sought as independent business owners.
3. **Franchisees are dependent on the performance of other franchisees in the chain.** A franchisee can benefit from the successes of other franchisees. But if other franchisees run sloppy operations, customer opinions of the chain will decline. As a result, customers may stop going to a franchise, even if a particular store maintains high standards.

NETBookmark

Breadsmith is a growing bakery franchise specializing in European-style breads and rolls. Access school.cengage.com/entrepreneur/ideas and click on the link for Chapter 7 to learn more about this franchise. When did the first Breadsmith franchise store open? What is the minimum amount a franchisee can expect to invest to open a Breadsmith store? How much of this is the franchise fee? What royalty fees must be paid to the franchisor?

school.cengage.com/entrepreneur/ideas



4. **The franchisor can terminate the franchise agreement.** If the franchisee fails to pay royalty payments or meet other conditions, the investment in the franchise can be lost. Similarly, when the franchise expires, the franchisor can choose not to renew the agreement.

Checkpoint

What should you consider when evaluating a franchise opportunity?

Enter a Family Business

The U.S. economy is dominated by family businesses. According to some estimates, as many as 90 percent of all businesses, including the vast majority of small- and medium-sized companies, are owned by families. Many large companies, such as Wal-Mart and the Ford Motor Company, continue to be owned largely by people who are related to the company founder.

Advantages of a Family Business

Entrepreneurs who work for their family businesses enjoy the pride and sense of mission that comes with being part of a family enterprise. They also enjoy the fact that their businesses remain in the family for at least one more generation. Some enjoy working with relatives and knowing that their efforts are benefiting others whom they care about.

Josh Morgan runs Morgan's, a restaurant that has been in his family for three generations. In his grandfather's time, Morgan's was a simple coffee shop, catering to people in the neighborhood. Thanks to changes made by Josh's mother, Mary, Morgan's became a fashionable lunch spot for people from all over town. When Josh took over, he carried on some Morgan traditions and implemented some new ideas, such as a gourmet take-out department. Josh takes great pride in seeing how the restaurant has evolved. He enjoys the thought that one day his grandchildren may hang pictures of him on the walls of the restaurant that will then belong to them.

did you KNOW?

According to the University of Southern Maine's Institute of Family-Owned Businesses, 35 percent of Fortune 500 companies are family controlled. Family businesses account for 50 percent of U.S. gross domestic product. They generate 60 percent of U.S. employment and 78 percent of all new job creation.

Disadvantages of a Family Business

Family businesses have several drawbacks. Family members, regardless of their ability, often hold senior management positions. This sometimes means that poor business decisions are made. It also makes it difficult to retain good employees who are not members of the family. Family politics often enter into business decision making. Also, the distinction between business life and private life is blurred in family-owned businesses. As a result, business problems end up affecting family life as well.

Entrepreneurs who do join their family business must be prepared to make compromises. Unlike individuals who start or buy their own companies, people who work for their families cannot make all decisions themselves. They may also be unable to set policies and procedures as they like.

Another challenge for a family-owned business is what to do when there is no family member to take over the business. This leaves the family with a decision to make regarding continuing the business or selling it to a nonfamily member.

Checkpoint

What are some of the advantages and disadvantages of entering a family business?

Starting Your Own Business

For one reason or another, joining a family business or operating a franchise may not be possible for you, or you might not be able to find a business to purchase. This means that to be an entrepreneur you will have to establish a business of your own. You need to consider the many advantages and disadvantages of starting your own business.

Advantages of Starting Your Own Business

Entrepreneurs who start their own business get to make decisions about everything from where to locate the business to how many employees to hire to what prices to charge. They are completely independent and create their own destinies. Many entrepreneurs find great satisfaction in starting their own businesses. Many are attracted to the challenge of creating something entirely new. They also get a feeling of triumph when their business turns a profit.

Disadvantages of Starting Your Own Business

There are many risks to consider when you start your own business. You must estimate demand for your product or service. There is no certainty that customers will purchase what you offer. Entrepreneurs who join family businesses, buy an existing business, or buy into franchises do not have this uncertainty because it is already known that customers will buy the product or service.

Entrepreneurs who start their own business must also make decisions that other types of entrepreneurs need not make. These decisions include what product or service to offer, the location, what employees to hire, and so forth. What may seem to be good decisions at the time may not always have positive results.

Lucy Donnelly realized how difficult it is to start a new business when she opened a kitchen accessories store. Lucy had considered purchasing a store franchise but had ruled it out because of the high franchise fee. Lucy's problems began when she realized that her customers did not consider her location to be convenient. As a result, fewer customers shopped in the store than Lucy had projected.



What things should you take into consideration before you start a business?

© Getty Images/PhotoDisc

Contacting suppliers was more difficult than Lucy anticipated, and many of them proved unreliable. The high-priced items Lucy purchased in the hope of increasing profits did not sell well.

Checkpoint

Why is it more difficult to start a new business than to take over an existing business or purchase a franchise?

7.1 Assessment

THINK ABOUT IT

1. When you purchase an existing business, why is it important to know the owner's reason for selling?
2. What extra expenses could you expect to pay when operating a franchise as compared to operating a nonfranchised company? Could you save money in expenses by operating a franchise? If so, how?
3. Your family owns a successful business that distributes flowers from around the world to local florists. Both of your parents work full time in the business. They have offered you a position in the company after you graduate from college. Will you accept their offer? Explain.
4. What would be the greatest advantage of starting a new business from scratch? What would be its greatest disadvantage? Do you think the advantages outweigh the disadvantages? Why or why not?

MAKE ACADEMIC CONNECTIONS

5. **COMMUNICATION** Interview an owner of a family business. Find out how long the business has been in operation and how many family members are employed in the business. Ask the owner what the advantages and disadvantages are of owning a family business. Compare this list to the advantages and disadvantages discussed in the text. Write a report on your findings.
6. **RESEARCH** Identify a franchise that interests you. Research the franchise and evaluate it using the ten points given in this lesson. Write a short report on your findings and conclude with your opinion on whether this franchise is a good opportunity.



TEAMWORK

Form teams. Brainstorm a list of reasons business owners may decide to sell their businesses. Put a check mark next to the reasons that could negatively affect the buyer's chance for success.

7.2

Choose a Legal Form of Business

Goals

- List advantages and disadvantages of a sole proprietorship.
- List advantages and disadvantages of a partnership.
- List advantages and disadvantages of a corporation.

Terms

- sole proprietorship
- partnership
- corporation
- share of stock
- board of directors
- dividends

Focus on Small Business

Establishing ownership

Cheryl and Grayson are going to open a camp for dirt bike riders. It will be a place where people can come and ride their dirt bikes and camp out overnight. Their long-range plan includes building cabins on the property that can be rented to the bikers.

Grayson asks Cheryl, "Do you think we should operate our business as a partnership or a corporation since we can't be a sole proprietorship?" Cheryl thought about it awhile and said, "You know, Grayson, there is a chance that someone could get hurt and we would be responsible if the accident was on our property. Let's choose the form of ownership that would help protect us and others too!"

"Good idea, Cheryl. Let's start investigating and see what we can find!"

Work as a Team Why do you think the possibility of someone getting hurt would be a big concern for Cheryl and Grayson? What other considerations do you think business owners should have when choosing a legal form for their business?



© Getty Images/PhotoDisc

There are several forms of business ownership to consider.

Sole Proprietorship

Once you decide to start your own business, you must decide what type of ownership the business will have. A business that is owned exclusively by one person is a **sole proprietorship**. Sole proprietorships enable one person to be in control of all business aspects. Sole proprietorships may be very small businesses with just a few employees, or they may be large businesses with hundreds of employees.

Advantages of a Sole Proprietorship

The government exercises very little control over sole proprietorships, so such businesses can be established and run very simply. Accurate



© Getty Images/PhotoDisc

What might be some of the disadvantages of operating a restaurant as a sole proprietorship?

tax records and certain employment laws must be met, but these are usually the only forms of government regulation for a sole proprietorship. For this reason, the sole proprietorship is the most common form of ownership in the United States.

Disadvantages of a Sole Proprietorship

It can be difficult to raise money for a sole proprietorship. You are the only person investing money. You also bear the burden of all of the risks. If a sole proprietorship fails and debts remain, the entrepreneur's personal assets may be taken to pay what is owed.

Rachel Gibson learned this lesson the hard way. Last year, her clothing store went out of business, leaving \$42,000 in debt. Because Rachel had set up the business as a sole proprietorship, she had to sell some of her personal assets, including her car, to pay off the debt of the business.

Checkpoint

Why are sole proprietorships the most common form of business ownership?

Partnership

A business owned by two or more people is a **partnership**. Many entrepreneurs prefer to go into business with one or more partners so that they have someone with whom to share decision making and management responsibilities, as well as the risks involved with entrepreneurship.

Advantages of a Partnership

Running a business as a partnership means that you will not have to come up with all of the capital alone. It also means that any losses the business incurs will be shared by all of the partners. Like sole proprietorships, partnerships face very little government regulation.

Disadvantages of a Partnership

Some entrepreneurs do not like partnerships because they do not want to share responsibilities and profits with other people. They fear being held legally liable for the errors of their partners. Partnerships can also lead to disagreements and can end bitterly.

Partnership Agreement

When two or more entrepreneurs go into business together, they generally sign a partnership agreement. The purpose of the partnership agreement is to set down in writing the rights and responsibilities of each of the owners. A sample partnership agreement is shown on the next page.

GENERAL PARTNERSHIP AGREEMENT FORMING “SUNNY SIDE UP”

By agreement made this 21st day of September, 20--, we, Ana Ortiz, Keesha Gentry, and Thomas Chase, the undersigned, all of Palm Harbor, Florida, hereby join in general partnership to conduct a food service business and mutually agree to the following terms:

1. That the partnership shall be called “Sunny Side Up” and have its principal place of business at 2013 Sand Drive, Palm Harbor, Florida, at which address books containing the full and accurate records of partnership transactions shall be kept and be accessible to any partner at any reasonable time.
2. That the partnership shall continue in operation for an indefinite time until terminated by 90 days’ notice, provided by one or more of the partners indicating his, her, or their desire to withdraw. Upon such notice, an accounting shall be conducted and a division of the partnership assets made unless a partner wishes to acquire the whole business by paying a price determined by an arbitrator whose selection shall be agreed to by all three partners. Said price shall include goodwill, and the paying of same shall entitle the payor to continue the partnership business under the same name.
3. That each partner shall contribute to the partnership: \$22,000 for initial working capital and the supplies and equipment.
4. That in return for the capital contribution in item 3, each partner shall receive an undivided one-third interest in the partnership and its properties.
5. That a fund of \$75,000 be set up and retained from the profits of the partnership business as a reserve fund, it being agreed that this fund shall be constituted on not less than 15 percent of the monthly profits until said amount has been accumulated.
6. That the profits of the business shall be divided equally between the partners, that the losses shall be attributed according to the subsequent agreement, and that a determination of said profits and losses shall be made and profit shares paid to each partner on a monthly basis.
7. That the partnership account shall be kept in the First Florida Bank and that all withdrawals from same shall be by check bearing the signature of at least one of the partners.
8. That each partner shall devote his or her full efforts to the partnership business and shall not engage in another business without the other partners’ permission.
9. That no partner shall cause to issue any commercial paper or shall enter into any agreements representing the partnership outside the normal conduct of the food service business without notice to the remaining partners and the consent of at least one other partner, and further that all managerial and personnel decisions not covered by another section of this agreement shall be made with the assent of at least two of the partners.

IN AGREEMENT HERETO, WE ARE

Ana Ortiz

Keesha Gentry

Thomas Chase

Ana Ortiz Keesha Gentry Thomas Chase



The sample partnership agreement identifies the following:

1. Name of the business or partnership
2. Names of the partners
3. Type and value of the investment each partner contributes
4. Managerial responsibilities to be handled by each partner
5. Accounting methods to be used
6. Rights of each partner to review and/or audit accounting documents
7. Division of profits and losses among the partners
8. Salaries to be withdrawn by the partners
9. Duration of the partnership
10. Conditions under which the partnership can be dissolved
11. Distribution of assets upon dissolution of the partnership

Checkpoint

Name some of the advantages and disadvantages of a partnership.

WHAT WENT WRONG

Partnership Woes

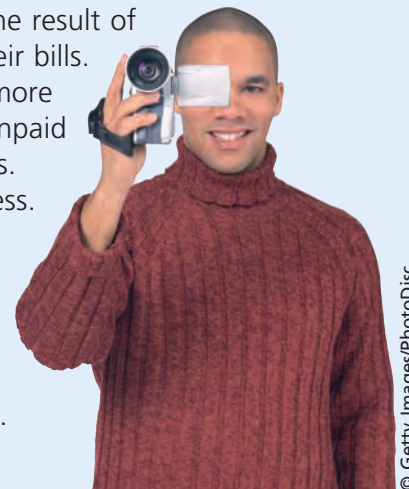
Stan and Peter met while working at a video production company. Stan was in charge of editorial and production. Peter ran the sales force. Stan decided to begin his own company and invited Peter to join him. SP Communications seemed like a perfect partnership. Peter would handle sales and administration, while Stan managed clients and directed production.

Things seemed to be going well until Peter decided he wanted to be a part of the creative process. He spent most of his time producing videos rather than looking for new business. Because of their friendship, Stan trusted that Peter was taking care of his side of the business.

As it turned out, Peter wasn't very good at the creative tasks he took on. He made mistakes that reduced expected profits. In addition, he wasn't making new sales contacts, which was supposed to be his main job.

By the time Stan realized what was happening to the business, it was too late. There weren't any new sales. What Stan thought

were profits were the result of Peter not paying their bills. Stan was left with more than \$150,000 in unpaid bills and other debts. Peter left the business. It took Stan three years to dig out of the financial mess and get his new company up and running successfully.



© Getty Images/PhotoDisc

Think Critically

1. How might Stan and Peter have avoided the problems that led to the end of their partnership?
2. Why is this situation a good example of the difficulty in maintaining partnerships between friends?
3. What types of things should be spelled out completely between partners at the beginning of the partnership?

Choose your partners wisely.

Corporation

A **corporation** is a business that has the legal rights of a person but is independent of its owners. A **share of stock** is a unit of ownership in a corporation. There may be many owners, who are called shareholders or stockholders. The corporation, not the owners, pays taxes, enters into contracts, and may be held liable for negligence.

Jim Munroe set up his company, Munroe Office Supply, as a corporation. He created 100 shares of stock worth \$1,000 each. Jim then issued 15 shares to each of three outside investors, which means they gave \$45,000 total to be shareholders in his company. Jim kept the remaining 55 shares himself. This means that Jim owns 55 percent of his company, while outside investors own a total of 45 percent of the company. The individual or group that owns the most shares maintains control of the company.

Every corporation has a **board of directors**, which is a group of people who meet several times a year to make important decisions affecting the company. The board of directors is responsible for electing the corporation's officers, determining their salaries, and setting the corporation's rules for conducting business. The board of directors also decides how much the corporation should pay in dividends. **Dividends** are distributions of corporate profits to the shareholders. The company's officers, not the board of directors, are responsible for the day-to-day management of the corporation.

Disadvantages of a Corporation

Setting up a corporation is more complicated than setting up a sole proprietorship or a partnership. To incorporate, you will need the assistance of a lawyer, who will help you file articles of incorporation with the state official responsible for chartering, or registering, corporations. Because of this, establishing a corporation can be costly. A business must be careful when it decides to incorporate. Articles of incorporation must be



© Digital Vision

What role does the board of directors play in a corporation?



written that fully detail the purpose of the business. If the articles are not written well, the corporation's activities can be limited.

Corporations are subject to much more government regulation than are sole proprietorships or partnerships. Another drawback of incorporation is that income is taxed twice. A corporation pays taxes on its income, and shareholders pay taxes on the dividends they receive from the corporation. This means that the corporation's profits are taxed as corporate income and again as individual income.

Advantages of Incorporation

If the corporate form of ownership is complicated and costly, why do entrepreneurs set up corporations? Liability is the main reason. Liability is the amount owed to others. The shareholders' risk is limited to the amount of money each shareholder invested in the company when he or she purchased stock. The personal assets of shareholders may not be taken to pay the debts of the corporation.

Munroe's Office Supply has gone bankrupt, leaving \$150,000 in debt. Each shareholder can lose only the amount he or she invested in the corporation, so the outside people who invested \$45,000 would lose their investment. Jim would also lose his investment of \$55,000. If Jim had set up his business as a sole proprietorship, he would have been liable for the \$150,000. If the business had been set up as a partnership among Jim and his friends, all four partners would have been liable for the \$150,000 debt.

Incorporation allows businesses to raise money by selling stock. Lenders are more willing to lend money to corporations than to sole proprietorships or partnerships. Because shareholders do not directly affect the management of a corporation, the main shareholder of the company can change through the buying and selling of stock without disrupting the day-to-day business operations.

S Corporation

A small corporation can elect to be treated as an S corporation. An *S corporation* is a corporation organized under Subchapter S of the Internal Revenue Code. Unlike regular corporations, an S corporation is not taxed as a business. The individual shareholders are taxed on the

profits they earn, as they would be in a partnership. Many companies establish themselves as S corporations because they lose money in their early years. The owners can use any losses suffered from the S corporation to offset other sources of personal income, and thus receive a tax break.

Chanda Patel works full time at a large company where she earns \$38,000 a year. She also runs Forever Yours, a wedding consultant business. Like many new businesses, Forever Yours lost money in its first year when its expenses exceeded its revenues by \$12,000. Since Chanda had

BE YOUR OWN BOSS

You have decided that you are going to start a new business giving horseback riding lessons. You need to decide which legal form you will use for your business. Choose a sole proprietorship, partnership, or corporation. Write a paragraph explaining why you chose the legal form you did and the advantages and disadvantages of your choice.

set up her company as an S corporation, she was able to reduce her taxable income by \$12,000. Her taxable income for the year was thus \$26,000 (the \$38,000 salary less the \$12,000 she lost on her business).

Limited Liability Company

A *limited liability company* (LLC) is a legal form of business that offers the limited liability protection of a corporation to its owners. The LLC is not subject to the rules for an S corporation and goes further than an S corporation in providing the benefits of partnership taxation and limited personal liability for all the owners of the business. The disadvantages of an LLC are that the type of businesses may be limited by state law, a single owner cannot establish an LLC, and many states limit the life of an LLC to 30 years.

Checkpoint

What is the main benefit of setting up your business as a corporation?

7.2 Assessment

THINK ABOUT IT

1. Which do you think is more risky: a sole proprietorship or a partnership? Why?
2. What would be the advantages and disadvantages of forming a partnership with a friend? Would you consider forming a business this way? Why or why not?
3. Why do you think the government regulates corporations more closely than it does sole proprietorships or partnerships?

MAKE ACADEMIC CONNECTIONS

4. **MANAGEMENT** You and a friend plan to open a business. Negotiate the terms of a partnership agreement. Using the Activity CD, open the activity "Partnership Agreement." Print a copy and complete the activity.
5. **MATH** Caren McHugh opened Best Foot Forward, a shoe store catering to women. To raise money, she organized her business as a corporation. She created 500 shares of stock, each worth \$75. Caren held 260 of the shares for herself. She sold the rest in equal amounts to six investors. How many shares does each investor own? If Best Foot Forward fails and leaves \$65,000 in debt, for how much would each investor be liable?



TEAMWORK

Working with teammates, create a chart listing all the forms of business ownership and the advantages and disadvantages of each one.



7.3

Legal Issues and Business Ownership

Goals

- Recognize how laws promote competition.
- Describe how to protect intellectual property.
- Identify consumer laws that affect businesses.
- Describe when and how a business owner should seek legal advice.

Terms

- intellectual property
- patent
- copyright
- trademark
- contract

Focus on Small Business

Why are there regulations?

James and Katie were starting an apparel company specializing in sportswear. They were trying to decide what they wanted their company logo to look like. "Let's put a 'swoosh' in our logo like the one Nike uses," James suggested.

"James, we can't use that logo. It's a Nike trademark," Katie responded. "See the TM symbol next to it. That means it's protected by a trademark and no one else can use it."

"Well, I guess we'd better keep thinking about what we want our trademark to be," answered James. "That's a good idea," Katie said. "And while we're at it, we'd better look into all the rules and regulations we need to follow. We don't want to start off on the wrong foot by doing something illegal."

Work as a Team Did you realize that businesses have to follow rules and regulations? Do you think it's fair for government to regulate business?



© Getty Images/PhotoDisc

Business owners must follow certain laws and regulations.

Regulations That Promote Competition

As an entrepreneur, there are laws that affect almost every aspect of your business. Even the competition that businesses face is regulated by the government. To make sure that competition is fair, the government has enacted various laws to help protect businesses.

Antitrust Legislation

Beginning in 1890, laws were created that made monopolies in certain industries illegal. A monopoly is also called a trust, so these laws were called antitrust laws. Antitrust laws also ban other types of business activities that do not promote competition. You should become familiar with these laws to determine how they affect your business.

SHERMAN ACT This law makes it illegal for competitors to get together and set prices on the products or services they sell. This means that you and your competitors cannot together decide to keep prices at a certain level. Discussing prices with competitors is illegal.

Pete Williams and José Pulido used to work together at Johnson Fencing, a business that installed residential fences. Each now owns his own fencing company. Last month Pete called José to see if he would raise his prices by the same amount Pete was planning to raise his prices. José told Pete he could not because fixing prices with a competitor is against the law.



© Digital Vision

How does antitrust legislation affect pricing?

CLAYTON ACT This law states that it is illegal for a business to require a customer to buy exclusively from it or to purchase one good in order to be able to purchase another good. A distributor of computers, for example, cannot make customers purchase software when they purchase a computer. Customers must be free to buy only the products or services they want from whom they want.

ROBINSON-PATMAN ACT This law protects small businesses from unfair pricing practices. It makes it illegal to discriminate by charging different prices to customers. A manufacturer, for example, may not sell its products at different prices to similar customers in similar situations when the effect of such sales will reduce competition. Differences in price may only be justified based on differences in quantities purchased (volume discounts), special distribution or legal requirements in different locations, or other economically sound reasons. If your business sells to other businesses, you must offer the same terms to all of those businesses. The law does not apply to retail stores where certain groups may be targeted by special promotions, such as giving discounts to senior citizens.

WHEELER-LEA ACT This law bans unfair or deceptive actions or practices by businesses that may cause an unfair competitive advantage. False advertising is an example. Under this act, businesses are also required to warn consumers about possible negative features of their products. Drug companies, for example, must let people know of any side effects they may experience from using a medication.

Government Agencies that Protect Competition

The Antitrust Division of the Justice Department and the Federal Trade Commission are two government agencies that work to make sure competition remains fair. Other agencies, such as the Federal Aviation Administration and the Food and Drug Administration, oversee business practices in particular industries.

JUSTICE DEPARTMENT The Justice Department's Antitrust Division takes legal action against any business it believes has tried to monopolize



an industry. It also prosecutes businesses that violate antitrust laws, which can lead to large fines and jail sentences.

FEDERAL TRADE COMMISSION The Federal Trade Commission (FTC) deals with issues that touch the economic life of every American. The FTC administers most of the laws dealing with fair competition and pursues vigorous and effective law enforcement. Some of the kinds of activities the FTC monitors include false or misleading advertising, price setting by competitors, price discrimination, and misrepresentation about the quality, composition, or place of origin of a product. It is the only federal agency with both consumer protection and competition jurisdiction in broad sectors of the economy. In addition, the FTC does the following:

- Advances consumers' interests by sharing its expertise with federal and state legislatures and U.S. and international government agencies
- Develops policy and research tools through hearings, workshops, and conferences
- Creates practical and plain-language educational programs for consumers and businesses in a global marketplace with constantly changing technologies

Checkpoint

How do laws promote competition?

Intellectual Property

Intellectual property is the original, creative work of an artist or inventor and may include such things as songs, novels, artistic designs, and inventions. Such works may be registered for special government protections—including patents, trademarks, trade names, and copyrights—that provide business owners with the exclusive use of the intellectual property in the United States and many foreign countries. Registration gives businesses or individuals the exclusive right to profit from what they have created. No one else can use their creations to make money. If you violate another person's patent, copyright, or trademark, you could be sued.

Patents

A **patent** is the grant of a property right to an inventor to exclude others from making, using, or selling his or her invention. The intent of a patent is to give the developer of a new product time to recover the development costs without having to worry about competition. Patents are issued by the U.S. Patent and Trademark Office and last for 20 years. During this period, no business or individual can copy or use the patented invention without the patent holder's permission. A *provisional patent application* allows an inventor one year to investigate the feasibility, marketability, and potential license interest of an invention before deciding to file a formal patent application. This gives the inventor the right to use the term *patent pending* and a head start on other inventors who may file for the same invention.



Copyrights

A **copyright** is a form of intellectual property law that protects original works of authorship, including literary, dramatic, musical, and artistic works. Copyright law does not protect facts, ideas, systems, or methods of operation. All books must have a copyright. A copyright lists the publisher of the work and the year in which the work was published. Copyrights remain in effect for 70 years after the death of the author.

Jessie Castille is a graphic artist who owns her own business. Jessie's copyrighted designs appear on T-shirts and posters. Last year, she found that a T-shirt manufacturer in another city was illegally using her designs. She sued the manufacturer for violating her copyright.

Trademarks

A **trademark** is a name, symbol, or special mark used to identify a business or brand of product. Products that are trademarked are identified by the TM or ® symbol. Examples include Band-Aid® and Kleenex®. You could not invent a new bandage and use the term Band-Aid in the product name. Nor could you use the “swoosh” mark that is trademarked by Nike in any product or business promotion you conduct.

Checkpoint

How can entrepreneurs protect intellectual property rights?

Famous Entrepreneur

Eli Whitney

Eli Whitney is best known as the inventor of the cotton gin, but a problem with intellectual property rights kept him from making his fortune from this invention.

Whitney obtained a patent for his invention but decided not to sell the machine to farmers. Instead, Whitney decided to install cotton gins throughout the south and charge farmers a hefty fee for processing the cotton himself. Resentful farmers made their own versions of the cotton gin and claimed they were “new” inventions. Due to a loophole in the 1793 patent act, Whitney was unable to win any lawsuits against the other cotton gin owners.

Without exclusive rights to the cotton gin, Whitney built another factory and began to make muskets

(guns) in a new way. Whitney invented tools and machines so that any worker could turn out uniform parts. The government was waiting for guns, and Whitney amazed everyone when he assembled guns from random piles of parts. Whitney had become the father of mass production in America! Eventually the arms factory made him rich, completing a success story for the boy who had shown mechanical aptitude by making a violin when he was 12 and selling handmade nails in his teens!



What led to Eli Whitney's success as an entrepreneur?

Think Critically

What do you think would have happened if Eli Whitney had obtained a patent for the cotton gin before others copied his machine?

Laws that Protect Consumers

The government also has regulations that protect consumers. Business owners should be aware of these laws.

Licenses

State and local governments require some businesses to have licenses. Beauty salons, restaurants, and health and fitness centers are just some of the companies that must carry licenses. If you own a business that requires a license, you and your employees may need to complete training requirements. You may also need to have regular inspections by state and local authorities. Failure to meet certain standards could mean the loss of your license and the closing of your business.



© Digital Vision

What problems might occur if an office park is built in a residential area?

Zoning Laws

Local governments often establish zoning regulations that control what types of buildings can be built in what areas. In many communities, certain areas are zoned for residential use only. This means that business buildings may not be built in those areas. Other areas may be zoned as commercial for retail businesses, as industrial, as agricultural, as multipurpose, and so on. All businesses must obey zoning regulations. Before you choose a location for your business, you will have to make sure that the area you have selected allows your type of business to operate there. Zoning laws help keep neighborhoods safe for its residents.

Consumer Protection Laws

A variety of laws and government agencies protect the public against harmful products. You will have to make sure that the products you manufacture or sell meet all consumer protection standards.

THE FEDERAL FOOD, DRUG, AND COSMETIC ACT OF 1938 This law bans the sale of impure, improperly labeled, falsely guaranteed, and unhealthful foods, drugs, and cosmetics. The Food and Drug Administration (FDA) enforces this law. The FDA has the power to force producers to stop manufacturing products that are unsafe.

THE CONSUMER PRODUCT SAFETY ACT OF 1972 This law sets safety standards for products other than food and drugs. When the Consumer Product Safety Commission determines that a product is unsafe, it can force businesses to recall the product and stop selling it.

THE TRUTH-IN-LENDING ACT OF 1968 This law requires all banks to calculate credit costs in the same way. When a consumer gets a loan, the lender must provide two types of information about the loan's cost—the finance charge and the annual percentage rate. The finance



charge is the total cost a borrower must pay for a loan, including all interest and fees. The annual percentage rate is the finance charge calculated as a percentage of the amount borrowed. These numbers help consumers evaluate alternatives and determine the best option.

THE FAIR CREDIT BILLING ACT OF 1974 This law is part of the Truth-in-Lending Act and helps consumers correct credit card billing errors. Consumers who feel they have been incorrectly charged must write to the credit card issuer and explain why they think the charge is wrong. The company must reply within 30 days and resolve the dispute within 90 days. While the disputed charge is being investigated, it cannot accrue interest.

This law also gives the consumer a method for resolving problems relating to product quality. The first step in dealing with a product of inferior quality bought with a credit card is to try to resolve the problem with the merchant. If it cannot be resolved, the consumer can withhold payment to the credit card company until the matter is settled.

Checkpoint

What laws protect the public?

When to Get Legal Advice

It is helpful to learn some basics about the laws affecting businesses so that you can handle minor legal issues yourself. Books and the Internet are good sources of information, or you could take a course in business law. However, there will be times when you will need to hire a lawyer for assistance. As an entrepreneur, you will need to decide when you should seek advice and when you can handle the situations on your own.

Hire a Lawyer

At some point, you probably will need to hire a lawyer. Your Chamber of Commerce may have a list of lawyers who specialize in small businesses. Other community business owners may also be able to suggest a lawyer. Lawyers can help you with a variety of legal issues.

HOW LAWYERS CAN HELP YOU		
Assist you in choosing a legal structure for your business	Create documents such as leases, purchase agreements, and contracts	Develop partnership agreements
Inform you of regulations and licenses	Give advice on insurance coverage	Advise you on taxes
Prepare and file patent applications	Help you plan for your future (a will, retirement plans)	Defend you in a lawsuit or file one on your behalf

Contracts

One of the most common reasons that a business hires a lawyer is to assist with contracts. A **contract** is a legally binding agreement between two or more persons or parties. As an entrepreneur, you will enter into



contracts as you start and operate your business. Contracts can be with suppliers, landlords, clients, and government agencies.

For a contract to be considered legally binding, certain elements must be included when the contract is created. These elements are agreement, consideration, capacity, and legality.

Agreement occurs when one party offers or agrees to do something and the other party accepts. Joni's Jellies has offered to sell Andy's Eatery two cases of homemade jelly each month for \$100 for a one-year period. Andy's Eatery responds by signing the offer and returning it to Joni's Jellies. Agreement is reached.

Consideration is what is exchanged for the promise. The \$100 check Andy's Eatery sends Joni's Jellies is consideration and causes the contract to be binding.

Capacity means the parties are legally able to enter into a binding agreement. Minors, intoxicated persons, and insane persons cannot enter into a binding contract.

Legality means that a contract cannot have anything in it that is illegal or that would result in illegal activities.

Checkpoint

What kinds of services can lawyers provide?

7.3 Assessment

THINK ABOUT IT

1. Think of three examples of how a business might misrepresent a product it sells. Explain each example.
2. Besides Band-Aid, Kleenex, and Nike, name at least three other products that are trademarked.
3. Explain the elements of the Fair Credit Billing Act.

MAKE ACADEMIC CONNECTIONS

4. **RESEARCH** Use the Internet, the newspaper, or your local library to find information on the process for applying for a patent. Also, find out how much a patent costs, how many patents have been issued to date, and what the criteria are for obtaining a patent. Prepare a short report on your findings.
5. **COMMUNICATION** Create an advertisement for a product that demonstrates a violation of the Wheeler-Lea Act.



TEAMWORK

Gather in teams. Make up several business scenarios that involve violation of antitrust laws. Role play scenarios for the rest of the class and let them tell which antitrust law is being violated.



Sharpen Your Entrepreneurial Skills

Effective Telephone Conversations

As you research business opportunities, you will need to make telephone calls to gather information. Once you become a business owner, you will conduct business over the telephone. The way you present yourself over the telephone will have a big impact on the people with whom you deal. It is also important to use good listening skills when talking on the telephone. Use the following tips to make the most of your telephone conversations.

1. **Speak clearly and talk directly into the receiver.** If you are using a headset, be sure that the microphone is in the correct position so that the person you are talking to will not have difficulty hearing you.
2. **Be cheerful.** Everyone prefers to deal with a happy person rather than someone who is sad or angry.
3. **Always speak politely.** Do not use foul or unprofessional language. Be respectful.
4. **Think about what you are going to say before you make a call.** Write down the questions you want to ask or the points you want to make. Consult your notes as you are talking to make sure you cover everything.
5. **Focus your attention on the person with whom you are talking.** Concentrate exclusively on what the person is saying. Ask questions to confirm you correctly interpreted what is being said.
6. **Eliminate all distractions.** Background noises, such as the radio and other people talking, should be held to a minimum.
7. **Take notes to summarize what you are hearing.** You may forget important details unless you write them down.



© Getty Images/PhotoDisc

TRY IT OUT

You found an advertisement for a candy store business in a local mall that is for sale. You want to call the real estate broker to find out more information about the business. Make a list of all the questions that you want to ask the broker. Role play the phone call with a classmate and make an appointment to visit the business and meet with the owner. Follow the tips listed above to ensure your telephone conversation is effective.

Chapter 7 | Assessment

SUMMARY

7.1 Decide to Purchase, Join, or Start a Business

1. An existing business has an established customer base and relationships with suppliers. The seller may train you, and prior records can make financial planning easier.
2. When evaluating a franchise opportunity, study the disclosure document, interview current owners, investigate the franchisor's history, investigate potential earnings claims, compare opportunities, get promises in writing, learn the risks of canceling the franchise, and seek advice from professionals.
3. Joining a family business has advantages, such as pride in the business and enjoyment of working with relatives. However, family politics can negatively affect the business.
4. Entrepreneurs who start entirely new businesses are completely independent and create their own destinies. However, there is increased risk because there is no established demand for the product or service and you must make all the decisions.

7.2 Choose a Legal Form of Business

5. A sole proprietorship is the easiest form of business ownership, but the owner may have trouble raising money for the business. Personal assets are at risk if the business fails.
6. A partnership is easy to start, faces little government regulation, and shares the risk with others. But a partner can be held legally liable for the actions of the other partner(s).
7. A corporation is more difficult to start, but it is easier to raise capital by issuing shares of stock. Owners' personal assets are not at risk.

7.3 Legal Issues and Business Ownership

8. Antitrust laws were developed to promote fair competition in business. The Antitrust Division of the U.S. Justice Department and the Federal Trade Commission are government agencies that work to ensure fair competition.
9. Entrepreneurs can protect intellectual property by registering for patents, copyrights, and trademarks.
10. Laws that protect consumers include licensing, zoning, and consumer protection laws.
11. You should learn about laws and regulations that affect your business. Lawyers can help with a variety of legal issues.

What do you know now?

Read Ideas in Action on page 177 again. Then answer the questions a second time. How have your responses changed?

VOCABULARY BUILDER

Match each statement with the term that best defines it. Some terms may not be used.

1. The original, creative work of an artist or inventor
2. Paid to the franchise company to support television, magazine, or other advertising of the franchise as a whole
3. The grant of a property right to an inventor to exclude others from making, using, or selling his or her invention
4. A business that has the legal rights of a person but is independent of its owners
5. Distributions of corporate profits to shareholders
6. A legal agreement that gives an individual the right to market a company's products or services in a particular area
7. The amount the local franchise owner pays in return for the right to run the franchise
8. A unit of ownership in a corporation
9. Weekly or monthly payments made by the local owner to the franchise company
10. A form of intellectual property law that protects original works of authorship, including literary, musical, and artistic works
11. A business that is owned exclusively by one person
12. A business owned by two or more people
13. A name, symbol, or special mark used to identify a business or brand of product
14. The costs associated with beginning a business
15. A legally binding agreement between two or more persons

- a. advertising fees
- b. board of directors
- c. contract
- d. copyright
- e. corporation
- f. dividends
- g. franchise
- h. initial franchise fee
- i. intellectual property
- j. partnership
- k. patent
- l. royalty fees
- m. share of stock
- n. sole proprietorship
- o. startup costs
- p. trademark

REVIEW YOUR KNOWLEDGE

16. Which of the following is *not* an advantage of buying an existing business?
 - a. existing customer base
 - b. prior records are available
 - c. seller can provide training
 - d. capital is required
17. **True or False?** A franchise is an inexpensive way to get into business quickly.
18. The legal form of business that is the simplest to establish is the
 - a. sole proprietorship
 - b. partnership
 - c. S corporation
 - d. limited liability company
19. **True or False?** The board of directors of a corporation is responsible for the day-to-day management of the corporation.
20. You and several other business owners in your area agree to raise the price of the paint you sell. You are in violation of the
 - a. Sherman Act
 - b. Clayton Act
 - c. Robinson-Patman Act
 - d. Wheeler-Lea Act

21. You want to advertise a special price on a product that you do not have just to get customer traffic into your store. If you do so, you will be in violation of the
 - a. Sherman Act
 - b. Clayton Act
 - c. Robinson-Patman Act
 - d. Wheeler-Lea Act
22. For a contract to be legally binding, it must have which of the following elements when it is created?
 - a. agreement, cooperation, capacity, legality
 - b. agreement, consideration, capacity, legality
 - c. agreement, consideration, cooperation, and legality
 - d. amendment, consideration, capacity, and legality
23. **True or False?** The U.S. Justice Department administers all of the laws dealing with fair competition.
24. **True or False?** A patent grants property rights to an inventor for 70 years.
25. Intellectual property rights can be protected by all of the following *except* a
 - a. copyright
 - b. license
 - c. patent
 - d. trademark

APPLY WHAT YOU LEARNED

26. You are meeting with the owner of an ice cream shop you would like to purchase. What specific questions are you going to ask her? What documents do you want to see? How will you evaluate whether or not to purchase this business?
27. You decide to start a business selling a new video game you have developed. You plan to sell the game over the Internet. What intellectual property right issues should you consider?
28. You want to purchase a cleaning service franchise. The franchise fee is \$19,500 and startup costs are \$15,200. Advertising fees are \$1,500. The royalty fee is 8 percent. If your estimated sales for the first year of operation are \$56,500, how much is your profit after paying all costs and the royalty fee?

MAKE ACADEMIC CONNECTIONS

29. **MATH** Marta Vasquez is one of three partners in a car dealership. The division of profits and losses as specified in the partnership agreement is 60 percent for Marta, 25 percent for the second partner, and 15 percent for the third partner. The dealership has recently lost a lawsuit and must pay damages of \$1,200,000. What is Marta's liability? What is the liability of each of the other two partners?
30. **COMMUNICATION** You are the owner of a coffee shop franchise. The franchise agreement specifies that the franchisee must submit all advertising plans for approval. Write a memo to the franchisor outlining your plan to market the franchise's new bagels.
31. **RESEARCH** Use the Internet, newspaper, magazines, and other materials to research business opportunities. Find two businesses for sale that interest you. Using the Activity CD, open the activity "Businesses for Sale." Print a copy and complete the activity.



Which business would be the better investment? Write a paragraph to explain your decision.

32. **HISTORY** Research one of the antitrust laws listed in Lesson 7.3. Write a brief history of what led to the passage of the law. Describe any amendments that have been made to the law since its original passage.
33. **GEOGRAPHY** China is a major source of intellectual property theft. Many counterfeit products are produced in China. Research the extent of this problem and learn how U.S. businesses can better protect themselves. Write a two-page report on your findings.

WHAT WOULD YOU DO?



You have purchased a copy of the newest version of the Windows operating systems for the computers in your office. It was expensive for you to update your systems, but you felt it was important to keep your equipment up to date. Your friend, Jeff, who is a sole proprietor and is struggling to get his business going, really needs the new version of Windows, but he does not have the cash to pay for it. He asks you if you would mind sharing your software license with him. What would you do?

BUILD YOUR Business Plan *Project*

This activity will help you continue with the development of a business plan for your business idea.

1. Contact your state and local governments and obtain information about licensing and zoning regulations. How will these regulations affect your business?
2. To expand your business, you have decided to purchase similar businesses in your area. List the businesses in your area that compete with you. Write the reasons you would or would not consider buying each business.
3. Find franchise opportunities available in your business field. Investigate one of these opportunities and gather information about it, such as franchise fees, royalties, projected earnings, and operating costs.
4. You have a friend who is interested in being your business partner. Write the partnership agreement for the two of you.
5. Make a list of all the advantages and disadvantages of organizing your business as a corporation. Determine how much stock to sell and the value of each share.
6. How will you become an entrepreneur? Will you buy an existing business, enter a family business, purchase a franchise, or start your business from scratch? Determine which form of business organization you will use—sole proprietorship, partnership, corporation, S corporation, or limited liability company. Write the ownership and legal structure section of your business plan as described in Chapter 3.

Planning a Career in Franchising



Business, Management
& Administration

"This weekend my family was really startled when we walked into a new restaurant to order sub sandwiches for lunch. Our former babysitter was behind the counter. She had bought the restaurant from a franchisor. The franchisor taught her how to run the restaurant. They provided the training and support materials she needed to successfully run her business. She said that, although the hours were long, the work was gratifying and profitable."

Why do people decide to purchase a franchise? How do they decide which type of franchise is best for them?

By helping individuals evaluate their personal and professional goals, franchise coaches help potential franchisees determine which franchise will best meet their needs. Coaches are usually compensated by the franchisors after a franchise is purchased by one of the coach's clients.

EMPLOYMENT OUTLOOK

- Faster than average growth is expected.
- Career changes, as a result of an evolving business environment and downsizing, will increase the need for business counselors.

JOB TITLES

- Franchise Business Coach
- New Business Sales Leader
- Franchise Business Consultant
- Franchise Performance Coach

NEEDED SKILLS

- A Bachelor's degree is recommended.
- Strong interpersonal and problem solving skills are needed.
- Prior management experience in training or sales is helpful.

- A desire to help others and an ability to gain their trust is important.

What's it like to work in Franchising? Jasmine, a Franchise Consultant, was speaking with a prospective new client who was eager to purchase a franchise. Jasmine was explaining the coaching process to her. By collecting data through informational interviews, assessments, and coaching sessions, Jasmine could help the client match her business objectives to an appropriate franchise.

Jasmine's next two phone calls were to two different windshield repair franchisors. Jasmine had a client whose testing results revealed that a windshield repair franchise was a strong match for his interests and business objectives. Jasmine was setting up a meeting between the franchisors and her client. After her client talked with both franchisors, Jasmine would coach him through the decision-making process. Jasmine would receive compensation from the franchisor her client selected.

On the way home from work, Jasmine stopped by a tutoring franchise that she helped one of her clients establish. She had a brief chat with the franchise owner to see if there were any business issues she could help resolve. By staying in touch with clients, Jasmine could help ensure the ongoing success of their franchise.

What about you? Would you like to provide structured testing and coaching to clients to help them match their interests, goals, and resources with an appropriate franchising opportunity?



BUSINESS LAW AND ETHICS MANAGEMENT TEAM DECISION MAKING EVENT

The Team Decision Making Event requires participants to analyze one or a combination of elements essential to the effective operation of a business. This event will require students to understand copyright laws, trademarks, and royalties paid to protected entities.

Your team has decided to open a sporting goods/gift shop in a popular university city. You want to sell merchandise that bears the emblem, logo, mascot, and name of the university. You have scheduled a meeting with the university's attorney (judge) to present your proposal for selling the merchandise. Your team must explain the pricing strategy for merchandise and demonstrate an understanding of royalties from merchandise sales to the university, college conference, and the National Collegiate Athletic Association (NCAA). You must also explain how your merchandise is different from university merchandise sold by competitors. You must convince the attorney that your business offers competitive advantages that will result in strong sales and good royalties for the university.

PERFORMANCE INDICATORS EVALUATED

- Explain the nature of business law.
- Describe legal issues affecting businesses.
- Describe strategies used to protect a business's copyrights.
- Explain legal strategies used to protect trademarks.
- Make an effective oral presentation.
- Explain legal considerations for pricing.
- Explain business ethics in product/service management.

Go to the DECA web site for more detailed information.

Think Critically

1. Why is it important to consider copyright and trademark laws when selling merchandise?
2. Why are copyright and trademark laws hard to enforce in other countries?
3. How can you determine the royalty percentage to be paid to a university for use of its emblem, logo, or mascot?
4. Why does a university need an attorney who specializes in copyright laws?

www.deca.org

Chapter 8

© PhotoDisc/Getty Images



Locate and Set Up Your Business

8.1 Choose a Location

8.2 Obtain Space and Design
the Physical Layout

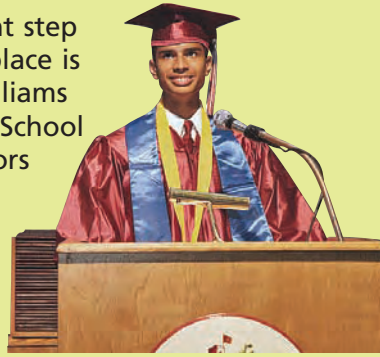
8.3 Purchase Equipment,
Supplies, and Inventory

school.cengage.com/entrepreneur/ideas

IDEAS IN ACTION

A Neighborhood Business

Choosing where to locate is an important step in opening a business. Often the best place is in your own neighborhood. When Ryan Williams was a 15-year-old student at Ossining High School in New York, he noticed that many neighbors wore headbands and wristbands with well-known logos. Ryan conducted an informal survey of his friends and found that many were interested in these products with a personal touch. He turned that idea into Rapappy, Inc., Personalized Headbands and Wristbands.



Ryan Williams, Rapappy, Inc.

© The National Foundation for Teaching Entrepreneurship

Because of his outstanding business plan and excellent communication skills, Ryan received a first-place award in the Entrepreneurship Business Plan Competition at the National Foundation of Teaching Entrepreneurship's (NFTE's) 2003 Summer BizCamp at the Fashion Institute of Technology. He also won the overall award for best technology use from the Goldman Sachs Foundation. Its Youth Entrepreneurship Expo is open to select students from around the country who excel in student entrepreneurship programs. At the Expo, students present their business plans and ventures to an audience of business professionals, parents, teachers, and judges. Ryan credits his EXPO participation with increasing his confidence and improving his speaking skills. The events helped Ryan realize that with planning and hard work, anyone can start and run a business.

Ryan appreciates the efforts of all the volunteers who gave of their time throughout his journey. Now a student at Harvard, Ryan realizes that these individuals helped nourish the entrepreneur within him. Ryan advises other young people who want to start a business to choose an area in which they are interested. He stresses the importance of taking risks, keeping good records, and persevering no matter how hard things seem.

What do you know?

1. Can you think of a good business opportunity for your neighborhood? Explain your ideas.
2. How did Ryan's participation in events help improve his entrepreneurial skills?
3. Why is the ability to persevere an important quality for an entrepreneur?

8.1

Choose a Location

Goals

- Examine options for locating a retail business.
- Discuss factors to consider when choosing a location for a nonretail business.
- Describe steps to take in selecting a site.

Terms

- industrial park
- enterprise zones
- trade area

Focus on Small Business

Good locations come at a price

Gail worked very hard to get just the right product mix for her company, Fitness For You, which offers creative branding strategies and products to the fitness industry. Business was good, but profits were still not at the level she wanted. She examined her expenses and realized that a large portion of her monthly expenses was for rental of her office space. She was located in an upscale office complex in Palm Beach, Florida. When she started looking at her customer base, she realized that most of her customer interaction was by phone or e-mail and at trade shows and business meetings held away from her office. Many of her customers were located in other states.

Work as a Team How important do you think Gail's location is to the success of her business? What would you advise her to do about her location?



© PhotoDisc/Getty Images

Carefully consider your location needs.

Locating a Retail Business

Making your product available in the right location to reach your target customer is very important. If you want to open a retail business, choosing the location for it will be one of the most important decisions you will make as an entrepreneur. The wrong location could spell disaster, but the right location will help your business succeed from the start. The right location for your business depends on the kind of business you plan to operate and the type of customer you want to reach.

Downtown Areas

In some communities, the downtown area represents an easily accessible, central location. Workers from downtown offices and professional



© PhotoDisc/Getty Images

★ Develop Your Reading Skills

As you read, make a chart showing the advantages and disadvantages of each type of location for retail, service, and home-based businesses.

What are the advantages and disadvantages of locating a business downtown?

businesses may shop at your business on their breaks or on their way to and from work. Rents vary widely from city to city, so you will want to do some research if you are thinking of using a downtown location.

Some downtown areas have lost business to neighborhood, community, and regional shopping centers. But many cities are revitalizing their downtown shopping districts and are offering incentives to attract businesses back into the area. Issues faced in many downtown areas include a higher crime rate, traffic jams, lack of free or convenient parking, and a lack of customers in the evening.

Neighborhood Shopping Centers

Neighborhood shopping centers are small shopping centers that serve a certain neighborhood. They are often called strip malls and consist of 3 to 15 stores. They are typically anchored by a supermarket, which is supported by other stores offering convenience goods (food, pharmaceuticals, and sundries) and personal services. Examples of supporting stores include drugstores, dollar stores, and dry cleaners.

Neighborhood centers represent good locations for stores selling goods or services that people need to purchase frequently. Rent is usually low in these centers, making them ideal for small businesses. Customers of neighborhood shopping centers are mainly residents of the surrounding area who shop at these centers because of their convenience. However, it could be a disadvantage for your business if the only customers you have come from the immediate area.

Community Shopping Centers

Community shopping centers have more square footage than neighborhood centers and are designed to serve residents from many neighborhoods. Apparel, furniture, toy, sporting goods, and electronic stores are often located in community shopping centers. Community centers



usually have one or two major anchor stores. Anchor stores can include the following:

- small department stores (Kohl's, JC Penney)
- discount department stores (Wal-Mart, Kmart, Target)
- large supermarkets (Kroger, Food Lion, Safeway, Publix)
- super drugstores (Walgreens, Rite Aid, CVS)
- home improvement stores (Home Depot, Lowes)

Although rent in community shopping centers is generally higher than in neighborhood shopping centers, it is usually still affordable. And stores in community shopping centers can earn higher profits. Anchor stores advertise heavily and attract customers from throughout the community. Other businesses in the shopping center typically benefit from the advertising. Customers shop at the anchor store and then may browse and buy at the smaller stores located in the shopping center as well.

Regional Shopping Centers

Regional shopping centers are designed to attract customers from an entire region. These large shopping areas usually have 40 to 100 stores and are anchored by one or more large department stores, such as Macy's and Nordstrom's. The majority of the stores sell apparel. Many regional shopping centers are malls. Regional shopping centers offer depth and variety of products and services.

If your business requires a large amount of walk-in traffic to be successful, you may want to locate in a regional shopping center. Rents at these centers are high, however, making it more difficult to earn profits. Also, the distance to the shop may be too great for some consumers. For convenience, they may decide to patronize businesses closer to their homes.

Super-Regional Shopping Centers

Super-regional shopping centers are the largest classification of shopping centers. They house more than 100 stores that offer an extensive variety of merchandise and services. They are typically anchored by three or more large department stores. They serve a larger population base than the other types of shopping centers. Two of the largest super-regional centers are the West Edmonton Mall in Edmonton, Canada (with over 800 stores), and the Mall of America in Bloomington, Minnesota (with over 500 stores).

Most tenants in these centers are large chain stores that can afford the very high rents charged. If convenience is a factor for your target market, customers may not be willing to travel a great distance to come to your store. Such centers usually are not recommended for new business owners because of the competition that exists among many similar businesses.

Stand-Alone Stores

Stand-alone stores can be located just outside of shopping centers or far away from other businesses. These stores often depend on drive-by traffic. They must have plenty of parking, good signs, and effective lighting if they are to be successful.



Businesses locate in stand-alone locations because rent is often less expensive than it is elsewhere. Also, a competing business is less likely to be right next door. Advertising is often necessary to earn a profit because people must have a reason to come specifically to your business. Large jewelers, auto parts stores, and flower and garden centers are often operated as stand-alone stores. A recent trend shows that department stores and large drugstores are opening up stand-alone stores.

Warehouses

Some retail stores, such as appliance dealers or furniture sellers, operate in warehouses. Warehouses are generally one of the cheapest rental facilities because they are of basic construction with few frills inside or out. Locating your business in a low-rent warehouse may allow you to charge lower prices than your competitors. However, locating away from other retailers can also mean that potential customers will not notice or be aware of you. For this reason, businesses that operate out of warehouses generally advertise heavily.



© Digital Vision/Getty Images

Why might an appliance store locate in a warehouse?

Checkpoint

What are the main options for locating a retail business?

Locating a Nonretail Business

Location can be very important for nonretail businesses, which include service, wholesale, and manufacturing businesses. Owners of these types of businesses face different considerations when choosing a location.

Service Businesses

For some service businesses, such as restaurants and hair salons, location considerations are the same as for many retail businesses. Owners of these types of businesses have to be very careful when choosing a location. Convenience can be an important factor for the business's customers.

Location is much less important for other types of service businesses. Customers never actually visit some service businesses, such as plumbing or carpet-cleaning companies. Locating these kinds of businesses in expensive areas does not make sense. Being close to customers may be important, however, because customers are more likely to call a company located nearby.



Eileen Whitman runs a small computer-repair service. Because most of her customers are businesses, Eileen chose a downtown location for her company. Being close to her customers means that she can quickly respond to emergencies and have clients' computers back in service the same day.

Industrial Businesses

Industrial businesses, such as manufacturing and wholesale companies, ship their products directly to their customers. This means customers rarely see their facilities. Operating in an upscale location that attracts lots of consumer traffic is not necessary for an industrial business. Availability of good employees and low cost are the key factors in determining where an industrial business locates.

Nonretail businesses sometimes locate in industrial parks. An **industrial park** is a section of land that is zoned for industrial businesses only. They are usually located where space is less expensive, away from housing developments and downtown areas. Communities sometimes subsidize rents in industrial parks in order to attract industrial businesses.

Tim Morrison's company specializes in preparing bulk mailings for large companies. Tim's corporate customers have their freshly printed catalogs and direct-mail advertisements sent directly to him from the printing companies. Using mailing lists provided by the customers, he prepares and ships the bulk mailings from his shop. All of Tim's contact with his customers takes place over the phone or via e-mail. There is no reason for him to locate his business in a prestigious part of town.

ENTERPRISE ZONES Industrial businesses may locate in enterprise zones. **Enterprise zones** are areas that suffer from lack of employment opportunities. Entrepreneurs who set up businesses in these areas may be eligible for favorable tax treatment based on the number of jobs their businesses create.

Some businesses may find the tax benefits offered by enterprise zones attractive. Others, however, may find that these benefits do not make up for the lack of an appropriate customer base or the increased risk of crime in those areas.



Why do you think the number of home-based businesses is growing?

Home-Based Businesses

In recent years, there has been an increase in the number of home-based businesses. Some of the reasons that entrepreneurs decide to locate their business in their home include the following:

- **Cost savings** Separate rent, utility costs, and maintenance fees for the business are eliminated, so there is more capital available for promotional activities and the purchase of inventory.

- **More freedom** Home-based business owners do not have to sign a lease agreement for the business, so they are not subject to the restrictions and obligations of a lease.
- **Convenience** The owner can work more flexible hours and does not have to commute to and from another location.

Locating their business at home is how many entrepreneurs get started. It is a great way to save money when starting a business. If the business outgrows its space, the owner can begin to look for an appropriate location outside the home.

Although it is cheaper to operate a business from home, there are some disadvantages to operating a home-based business. Lack of space can limit the expansion of the business. It may also be hard to keep your business and family life separate. Many home business owners feel isolated from the business community and miss opportunities to interact and network with colleagues.

Janet Lawson of The Healing Center began her therapeutic massage business in the basement of her home. As demand for her services increased, she needed more space for new equipment and employees. She leased space in her community and moved her business.

Checkpoint

What are some of the factors to consider when selecting a location for a nonretail business?

WHAT WENT WRONG

Right Space, Wrong Place

Jim Teal opened Jimmy T's Rib House, and within the first ten months, he was making profits. One day a commercial realtor advised Jim that a restaurant four times the size of his current space was on the market. The realtor said he could get Jim a good deal on the lease if he liked it.

Jim knew that the city where the building was located had no other barbecue rib restaurant. He researched and verified the population numbers and demographics for the geographical area. It was in a good neighborhood, on a main road, just off the freeway. He even did a traffic-flow study, and the numbers were terrific. The grand opening week went well, but then business began to drop off.

Although there was plenty of traffic, Jimmy T's was on the wrong side of the street. Customers coming west from the freeway exit could not cross the center island, and there was a "No U-Turn" sign at the corner. When Jim tried to

improve his visibility and signs to attract more freeway traffic, he found that city regulations prevented it. After six months, Jim took his loss and closed the new restaurant.

Think Critically

1. What questions about location should Jim have asked the realtor before assuming the lease?
2. Who else should Jim have questioned about the location?



© PhotoDisc/Getty Images

Consider the pros and cons of a location.

Select Your Site

Given all of the possible types of locations for different types of businesses, how do you decide where to locate? One way of identifying your options is to buy a map of your area and mark the trade area. The **trade area** is the area from which you expect to attract customers. Indicate on the map all of the locations that might be appropriate for your business. Also indicate the location of all of your competitors. Using a different color marker or symbol, mark the locations of businesses that do not directly compete with your business but may attract the same kind of customer. For example, if you want to open a poster store that will attract mostly teens, mark the locations of other stores that also appeal to this target market, such as trendy clothing stores and music stores.

Location Type and Availability

The next step is to identify which type of location is right for your business. Do you want to locate in a community shopping center? A stand-alone store? Downtown? At home? Determining which type of location you want will help narrow your search.

After deciding on the type of location, you must determine what spaces of this type are available in your trade area. The classified section of your local paper will list available sites. You can also find locations simply by driving around your trade area. Signs advertising an available building will often be hung in the front window or placed on the front lawn of the property. Web sites and search engines may also be helpful in determining what options are open to you. Mark each possible location you find on your trade area map.

Evaluate the Location

After getting a list of possible locations, inspect each location to assess its appeal. Is the location safe? Is it attractive? Does it seem to attract



© PhotoDisc/Getty Images

How can you find potential locations for your business?

the kind of customers your business will be targeting? Is it easy to reach? Is parking adequate? Do businesses in the vicinity seem to be thriving? After answering these questions you should be able to narrow down your choices to only one or two viable business locations.

Michele Kim is planning to open a fabric store. Convinced that there is a market for her product, Michele proceeds to identify the best location for her store. She rules out a downtown location because of the lack of parking and the fact that many shoppers are not willing to go downtown in the evenings. After thorough research, she settles on a community shopping center because of the low rent, the good parking, and the relative safety of the area.

Checkpoint

What are some of the factors you should consider when selecting a site for your business?

8.1 Assessment

THINK ABOUT IT

1. Why do you think rents are lower in neighborhood shopping centers than in community and regional centers?
2. Do you think advances in technology have played a part in some new business owners' decision to operate from their homes? Why or why not?
3. When marking the trade area for your business, why should you indicate the locations of your competitors?

MAKE ACADEMIC CONNECTIONS

4. **PROBLEM SOLVING** Using a map of your area, mark the potential trade area for a new furniture superstore. Then use the six-step problem-solving model to help determine at least two appropriate locations.
5. **COMMUNICATION** As a downtown business owner, you actively work to recruit other businesses to the area. Write a letter to the editor of your local newspaper about the advantages of locating a business downtown.



TEAMWORK

Gather in teams. Brainstorm a list of rules a home-based entrepreneur might make in order to be as effective and productive as possible while working at home. When sharing your rules with the class, ask one person from your group to write your rules on the board.



8.2

Obtain Space and Design the Physical Layout

Goals

- Compare purchase and lease options.
- Describe layout considerations for different types of businesses.

Terms

- tenant
- landlord
- gross lease
- net lease
- percentage lease

Focus on Small Business

Walking inventory

Trying to create a fun, relaxing atmosphere in his clothing and accessories store, Justin decided to move the cash register into the far back corner of his store. That gave him more space for displays and merchandise up front. He was really excited about all he could do with the space.

Due to slow traffic in the store at times, there was often only one employee on duty. The next thing Justin knew, his inventory was “walking right out the door,” and it wasn’t with paying customers. Justin had created a perfect layout for shoplifters. He knew he had to make some changes.

Work as a Team What did Justin do wrong in changing the layout of his store? If Justin wants to keep the same layout, what suggestions can you make that would cut down on shoplifting?



© PhotoDisc/Getty Images

The layout should meet the needs of the business and its customers.

Lease or Buy Space

Unless you operate your business out of your home, you will have to lease or buy business property. There are advantages to buying space. Owning property offers a bigger tax advantage than leasing. Owning the building that houses your business allows you a tax deduction on the interest you pay on your loan. And a loan payment on the building may be no more than a lease payment.

However, most entrepreneurs lack the money to purchase property for their businesses. Even entrepreneurs who can afford to purchase property generally prefer not to be locked into a particular location. Some leases require the owner of the building, not the owner of the business, to pay certain expenses, such as upkeep and maintenance of the building’s exterior. For these reasons, most businesses lease space.

Commercial Leases

When leasing property, a contract is needed. In a lease contract, there is a tenant and a landlord. The **tenant** is the person who pays rent to occupy

space owned by someone else. The **landlord** is the person who owns and rents out buildings or space. There are three kinds of commercial leases.

1. In a **gross lease**, the tenant pays rent each month for the space occupied, and the landlord covers all property expenses for that space. Expenses such as property taxes, insurance on the building, and building maintenance are paid by the landlord.
2. A **net lease** occurs when the landlord pays building insurance, and the tenant pays rent, taxes, and any other expenses.
3. With a **percentage lease**, the tenant pays a base rent each month, and the landlord also receives a percentage of the tenant's revenue each month. The percentage lease is most common for prime retail locations. This type of lease can be beneficial for both the landlord and tenant. The landlord shares in the business's profits, and the tenant has the advantage of a lower base rent, which can make rent more affordable during slow sales periods.



© Digital Vision/Getty Images

Why is it important to have a contract when leasing property?

Commercial lease agreements are usually long and complex. You should never sign one without consulting an attorney. Your attorney will review your lease to make sure that it covers all conditions and costs, including the basic rent, maintenance fees, utility costs, insurance costs, and other items.

Compare Costs of Doing Business

Once you have selected some possible locations for your business, you need to compare the costs and benefits of leasing property at each location. To do so, you need to calculate how much rent you will be paying per customer.

Juan Martinez plans to open a music store. He looks for a location that is convenient, far from other music stores, and safe for customers. He finds two locations that meet his needs—one in a neighborhood shopping center and the other in the downtown area.

CALCULATING RENT PER CUSTOMER To decide which location he should select, Juan determines the amount of rent he would pay and the number of projected customers for each location. Juan divides the amount of rent by the number of projected customers to determine the rent per customer.

	Downtown	Shopping Center
Rent per month	\$ 925	\$ 1,100
Projected customer traffic per month	÷ 8,500	÷ 12,000
Rent per customer	\$ 0.11	\$ 0.09

From his calculations, Juan determines that, although the total rent will be higher, he will be paying a lower rent per customer at the shopping center. Juan leases space at the shopping center.

Checkpoint

Name three kinds of commercial leases.



did you KNOW?

According to a recent report by IGD, a consumer and shopper research company, 35% of shoppers visit only the aisles which they believe have the items they need. This indicates the importance of placing new products or promoted items in key locations to ensure good product exposure.

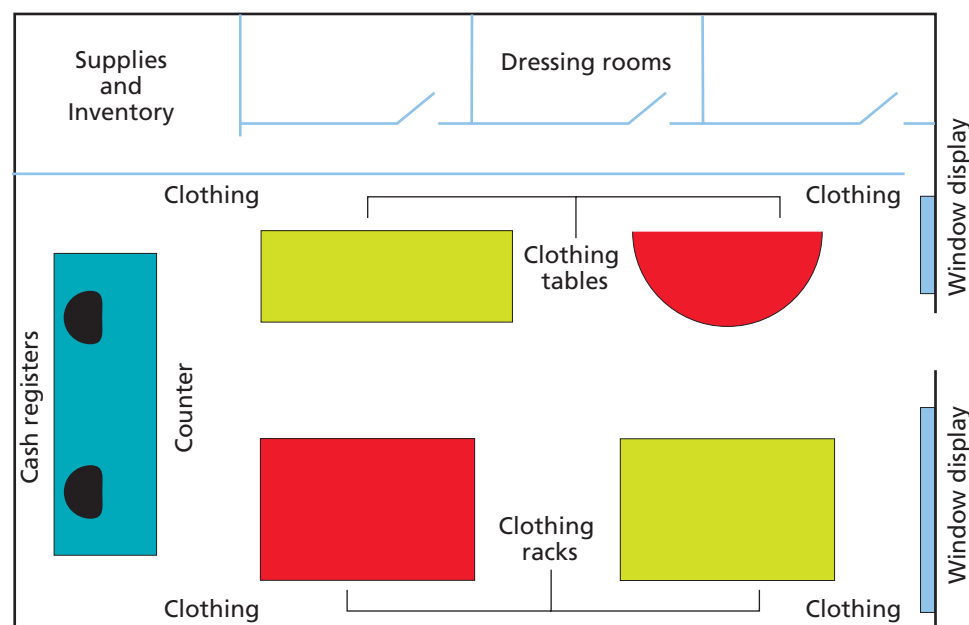
Design the Layout of Your Business

After you have leased or purchased a facility, you will need to design your layout, or floor plan. Your layout must include enough space for employees, customers, merchandise, and equipment. It must also have space for restrooms, stockrooms, storage, and offices.

Create the Floor Plan

You will need to prepare a scale drawing of the layout. Graph paper will help you draw your layout to scale. To create a scale drawing, let 1 inch represent 1 foot of actual space. For example, a 4-foot-by-3-foot closet would be represented by a 4-inch-by-3-inch rectangle. Indicate the planned use of each area. Also indicate the location of furniture, display cabinets, shelves, fixtures, and equipment. Your drawing will help you identify potential problems in your layout. It will also help you communicate with the people who may be helping you organize your space.

Sample Floor Plan



Decide on a layout, an outside sign, and window displays that match your image. If you sell expensive jewelry, you will probably decide on a sophisticated outside sign and an elegant inside design that will appeal to your target customer. If you sell outdoor equipment, you will select a very different design for your store.

Layout of a Retail Business

For a retail business, appearance is very important. A store with inviting window displays and creatively displayed merchandise sends a positive message. A store with crowded aisles and piles of sale items does not. The goal of your layout should be twofold. It should attract customers to your store and keep them coming back, and it should meet the needs of your business.

Here are some ways you can send a positive message about your store.

1. Choose lighting that is appropriate for the kind of merchandise you sell. Good lighting is important for any business where customers inspect merchandise closely. Avoid fluorescent lighting, which creates an unattractive glare.
2. Think carefully about window displays. Use them as a way to display new merchandise or seasonal items.
3. Make the entrance inviting. An entrance that is welcoming will draw customers into the store.
4. Use common sense when organizing the merchandise in your store. Customers should always easily find what they want. Inventory and supplies should also be well organized so that you can find things faster and serve your customers better.
5. Leave at least four feet of aisle space. This makes it easy to move around in your store.
6. Create attractive in-store displays. Customers are drawn to displayed merchandise.

Famous Entrepreneur

Rachael Ray

Sometimes success comes from being in the right place at the right time. And it always helps to be prepared! Just ask Rachael Ray, who says her life has been “a very happy, wonderful accident that I didn’t and couldn’t have planned.”

The truth behind that statement is that Ray had extensive training in the food service industry before she became a TV star. Starting at the candy counter of Macy’s, she was promoted to manager of the Fresh Foods Department. She then helped to open and was store manager and buyer for Agata & Valentina, the prestigious New York gourmet marketplace.

She was discovered by the local CBS station while working for Cowan & Lobel, a large gourmet market in Albany, NY. She had begun a series of cooking classes

to increase sales during the holidays. The classes were so popular, the station signed her on to do a weekly “30 Minute Meals” segment for the evening news. She sold 10,000 copies locally of a companion book.

The Food Network soon came calling and the *Rachael Ray Show* began in September 2006. Her personality and quick, tasty recipes fit modern lifestyles.

Think Critically

Even though Rachael Ray says the way her life has turned out has been accidental, what steps did she take in her life that prepared her for her current position?



© Brad Barker/Getty Images

How did Rachael Ray build upon her early success?

NETBookmark

Appearance is very important for a retail business. Effective store layouts maximize the available space and create a natural flow of traffic through the store to encourage additional spending. Access school.cengage.com/entrepreneur/ideas and click on the link for Chapter 8. Read the article on types of store layouts. According to the article, what three factors must a retailer consider when developing a floor plan/store layout? Name the five types of store layouts described in the article. Then think of a retail store you visit frequently. Which type of layout design does the store use?

school.cengage.com/entrepreneur/ideas

7. Use wall space wisely. Wall space may be too high for customers to reach, but it can be used to display merchandise.
8. Place the cash register in a central location. Customers should not have to search for a cashier.

Layout of a Service Business

Service businesses can be divided into two categories.

- Service businesses where people come to the business location to receive a service (restaurants, hair salons, automobile repair services)
- Service businesses that travel to the customer's location and perform the service on-site (exterminators, plumbers, cleaning services)

The layout of the first type of service business should be considered just as carefully as that of a retail business. However, on-site service businesses are never visited by their customers, so an attractive layout is not important. Organization should be a major consideration of on-site service businesses so that supplies and other items are easy to find.

Layout of a Wholesale Business

Customers of wholesale businesses are concerned with price and quality, not physical appearance. For this reason, a wholesale business needs only to be well organized. Wholesalers are constantly receiving and shipping large volumes of products. Wholesale businesses can do the following to facilitate shipping and receiving:

1. Locate in a one-story warehouse.
2. Keep merchandise close to the shipping dock. This minimizes the distance it will have to be moved when it is brought into and taken out of the warehouse.
3. Store the most popular items in the most accessible locations.
4. Have areas that can accommodate merchandise of all sizes.
5. Keep walkways free of merchandise so that employees can exit the building quickly in the event of an emergency.
6. Store items safely. For instance, do not stack too many boxes on top of one another because they may fall if they become unsteady.

Layout of a Manufacturing Business

For manufacturing businesses, efficiency, not attractiveness, is what counts. Other important considerations include the following:

1. Work teams should be situated close together.



2. Supervisors should be able to easily observe the people they supervise. Their office should be located near the employees.
3. Exits should be clearly marked and easily accessible so that employees can quickly leave in the event of an emergency.
4. Any hazardous materials should be stored safely.
5. Equipment and machinery should be positioned in a way that reduces the chance of an accident.

Checkpoint

What are the major considerations for choosing a layout for a business?

8.2 Assessment

THINK ABOUT IT

1. What are the differences between a gross lease, a net lease, and a percentage lease? Which type of lease would you prefer? Explain why.
2. Why do you think it is important to draw a floor plan of your business before you begin setting up shop?
3. For a service business that serves customers at the place of business, why are layout considerations similar to those for a retail store?

MAKE ACADEMIC CONNECTIONS

4. **RESEARCH** You are thinking about opening a bicycle sales and repair shop. Research layouts of other bicycle shops and determine what type of equipment and supplies would be included in the layout for this shop.
5. **MATH** Determine the rent per customer for the following:

Location	Rent per Month	Projected Customer Traffic per Month	Rent per Customer
Downtown	\$1,200	9,500	?
Community shopping center	\$2,800	18,000	?
Stand-alone store	\$1,050	7,400	?



TEAMWORK

Working with a team, choose a business with which you are familiar. Using the Activity CD, open the activity "Evaluate the Layout of a Business." Print a copy and complete the activity to rate the effectiveness of the business's layout.



8.3

Purchase Equipment, Supplies, and Inventory

Goals

- Explain how to find and choose vendors for your business.
- List factors that determine the needed level of inventory.

Terms

- inventory
- vendors
- quote
- reorder point

Focus on Small Business

Setting up shop

Karen had operated Bear Creek Embroidery and Alterations as a home-based business for several years. Her business had grown to the point that she needed more space for equipment and new employees. She shopped around for space and found a good location near her neighborhood.

While planning the move, Karen realized that in addition to rent, she would have many other expenses now that she would no longer be operating out of her home. As she began to add up the cost of all the furnishings, equipment, supplies, and other expenses that she would incur by moving out of her home and expanding her business, she began to wonder if she could afford the move.

Work as a Team What additional expenses will Karen be paying if she moves her business out of her home? Before deciding to move her business, what should Karen have done to be sure she could afford the move?



© PhotoDisc/Getty Images

Consider all of the expenses involved in running a business.

Obtain Equipment and Supplies

Every business needs equipment and supplies. Many businesses also need inventory. Machinery, computers, cash registers, and furniture are types of equipment. Supplies include things like paper, pens, and pencils. **Inventory** is the merchandise a business sells to its customers. Without these things, a business cannot function properly. If there is no inventory, what will you sell? If there is no paper, how will you send a letter? Suppliers or vendors can provide your business with everything you need to function.

To determine the equipment and supplies you need to start your business, make a list of what you think you will need. All businesses need standard items such as furniture, lamps, and office supplies. Businesses also need special items specific to the type of business. For

example, lawn-care companies and landscaping firms would need lawn fertilizer as part of their supplies and lawn mowers as part of their equipment. Your list should include standard items needed by all businesses as shown in the table below. It should also include items specific to your particular business.

Once you have listed all of the items you need, indicate how much of each item you require. Be sure to list the minimum quantity you need right now, not the amount you might need if your business succeeds. Being overly optimistic could leave you with many bills that will be difficult to pay if your sales fall short of your projections.

STANDARD EQUIPMENT AND SUPPLY NEEDS FOR MOST BUSINESSES	
Type	Items
Furniture	Desks, chairs, bookcases, filing cabinets, tables, computer stands
Fixtures	Lamps, overhead lights
Office Equipment	Computers, routers, modems, fax machines, telephones, printers, copiers
Office Supplies	Stationery, pens and pencils, scissors, tape, staplers, paper clips, binder clips, folders, calendars
Maintenance Supplies	Toilet paper, paper towels, hand soap, cleaning supplies
Kitchen Supplies	Coffee maker, small refrigerator, soft drinks, coffee, tea

Identify Suppliers

To fill the standard and special needs of your business, you will need to research vendors. **Vendors** are companies that sell products and services to businesses. Vendors are also called *suppliers*. Valuable sources of vendor information include the following:

- Telephone directory advertising section
- Trade magazines (specialized magazines devoted to a particular industry), which carry vendor advertising
- Trade associations
- The Internet
- Other companies in your industry

Shira Silberg wants to open an assisted-living center for senior citizens. To find suppliers of furniture, linens, and many other items, Shira looks through copies of trade magazines for advertisements from companies that target the nursing-home industry. Shira also locates vendor web sites for additional information. Finally, she contacts other assisted-living centers to find out which vendors they use.

Evaluate Proposals

Most of the items you will need to start your business will be available from a variety of vendors. How will you decide among them? Before you make a purchase, contact several vendors and ask them to quote you





© Digital Vision/Getty Images

Why is it important to have a reliable vendor?

a price for the merchandise you are interested in purchasing. A **quote** is an estimate for how much you will pay for the merchandise or service. Also ask vendors about the quality of their merchandise, their financing terms, quantity discounts, and shipping and handling charges. Once you have all the information you need, compare the various proposals. Choose the vendor that provides the best combination of products at a cost that fits your budget.

Shira selects her suppliers by asking for proposals from the vendors that appeal to her the most. She then compares price quotes, service, quality of merchandise, and discount options. Shira knows that the lowest price is not always the best option if paying a little more means receiving better quality and service. She decides on a higher-priced linen business because it offers additional services that meet the needs of her business the best.

Checkpoint

What should you consider when selecting vendors for your business?

Purchase Inventory

Retailing, wholesaling, and manufacturing businesses must purchase inventory before they can open for business. For retail and wholesale businesses, inventory is merchandise purchased with the intent of reselling it to customers. For manufacturing businesses, inventory also consists of the parts that will go into producing the business's product as well as its finished goods.

Purchase Inventory for a Startup Business

Determining the amount of inventory to keep in stock is difficult for all business owners. It is particularly difficult for owners of new businesses, who do not yet know what their level of sales will be.




Chris Keating wants to open an art supplies store. He wants to have enough inventory that his shelves look full. He also wants to be able to offer his customers a full line of art supplies. Not knowing how high or low his sales will be at first, Chris doesn't want to purchase too much inventory. He doesn't want to tie up his cash in inventory if he can't sell it quickly. Chris is also worried about finding space to store the inventory. Because of these concerns, Chris purchases just enough stock to fill his shelves.

Purchase Inventory for an Ongoing Business

Once your business is up and running, you will have a better idea of how much inventory you need. To make sure that you do not run out of stock unexpectedly, you can establish reorder points for each product you sell. The **reorder point** is a predetermined level of inventory that signals when new stock should be ordered. How low you set the reorder point depends on how long it takes your supplier to get merchandise to you, how many units of the item you sell each month, and how important it is for you not to be out of stock.

Chris sells 150 erasers a month. Because he never wants to be out of stock, he sets his reorder point at 30. Every time his inventory of erasers falls at or below 30 units, he places an order to renew his stock of this item.


BE YOUR OWN BOSS

You own a toy store. You specialize in collectible dolls and stuffed animals. Some of the stuffed animals that you carry have become very popular with children, and you cannot keep them in stock. In the past, your reorder point was three and you never ran out of the animals, but now you are losing sales because of empty shelves. You know you could sell more stuffed animals if you had them. Outline a plan that will meet your business's inventory needs as well as your customers' needs.

Checkpoint

How do you determine the amount of inventory to keep in stock?



© PhotoDisc/Getty Images

Why should you keep track of your inventory?



8.3

Assessment

THINK ABOUT IT

1. Why should you make a list of all the equipment and supplies you need to start your business?
2. Why is it important to obtain price quotes from several different vendors before selecting a vendor? What questions should you ask potential vendors?
3. What issues should a business owner consider when purchasing inventory for the business? Explain the relationship between inventory and customer service.

MAKE ACADEMIC CONNECTIONS

4. **COMMUNICATION** You are a wholesale distributor of party supplies. A new store, Party Express, has asked you to submit a proposal for supplying its paper goods inventory. In order to prepare for a meeting with the Party Express management, make a list of questions you will ask them in order to get enough information for your proposal. Role play the meeting with a classmate.
5. **MATH** Using the Activity CD, open the activity "Equip Your Business." Print a copy and complete the activity to calculate the cost of the equipment and supplies you would need to start your own fitness training business.
6. **RESEARCH** Use the Internet, trade magazines, newspapers, and other sources to search for suppliers of house paint for professional painters. Report your research in a short document which could be used by a painter to help select a vendor.

**TEAMWORK**

Lee Torres is opening a retail pet store. The store will carry high-quality pet foods, leashes, collars, coats, carriers, beds, toys, treats, grooming supplies, and flea products for both dogs and cats. Lee does not plan to sell puppies or kittens but will have a large assortment of birds, tropical fish, and small animals (hamsters, guinea pigs, etc.) and the foods and accessories needed for them. The store will carry an assortment of books about selecting, training, breeding, and caring for pets. In addition, Lee will also offer grooming services for pets.

Working with teammates, make a list of all of the equipment and supplies Lee will need for his business. Use the Internet to compile a list of several vendors that sell pet products and supplies. Create a list of questions that Lee should ask the vendors to help him select the best vendor. Finally, consider Lee's inventory needs. Decide which products Lee should order in large or small quantities and explain why. Compile a report with all of the information you have gathered to present to Lee.



Sharpen Your Entrepreneurial Skills

E-Mail Etiquette

As you deal with vendors and suppliers, you will have the opportunity to communicate using e-mail on a regular basis. Today, many business deals are made by e-mail without the parties ever meeting or talking over the telephone. E-mail is preferred over regular mail, fax machines, and telephones as being quicker and less intrusive than a phone call. With e-mail, you can key your message into the computer, and with one stroke, your message is delivered instantly.

Although it may not be as formal, the same care should be given to e-mail as to the preparation of a business letter. You should always proofread your e-mail for spelling and grammar before sending it. Other guidelines to remember when sending e-mails include the following:

1. **Cover only one topic per e-mail.** If you have several topics to discuss, send them in separate e-mails.
2. **Use an appropriate subject line.** The subject line should appropriately describe the message. Also, because people receive numerous e-mails, try to use a subject line that will catch their attention.
3. **Your message should be brief.** Use short sentences and paragraphs. Long e-mails often go unread.
4. **Be courteous and professional in your message.** Remember, once the e-mail is sent, you cannot get it back.
5. **Remember that business e-mail is not private.** E-mail is subject to being monitored in many companies. Also, any e-mail you send can easily be forwarded to someone else. Do not send anything that you would not want to be made public.
6. **Limit the number and size of attachments.** Large files can take too much time to open and can fill up the recipient's mailbox.

When it comes to e-mail, the best habit to have is to use e-mail etiquette that will display your professionalism to others. Be sure your e-mail is worthy of a response.

TRY IT OUT

You want to send an e-mail to a potential vendor asking for a quote for office supplies that you need for your new business. Compose the e-mail that you would send, using the guidelines given above.



© PhotoDisc/Getty Images

Chapter 8 | Assessment

SUMMARY

8.1 Choose a Location

1. Options for locating retail businesses include downtown areas, neighborhood shopping centers, community shopping centers, regional shopping centers, super-regional shopping centers, stand-alone stores, and warehouses.
2. Location factors to consider include parking, traffic, convenience, cost, demographics, draw of nearby stores, and competition.
3. When choosing a location for service businesses that customers visit, the same factors must be considered as for retail businesses. For service businesses where the service is performed at the customer's home or business, the business location is not as important.
4. For industrial businesses, availability of good employees and low cost are key factors in choosing a location.
5. Operating a small business out of the home can save on costs, but it may make it difficult to separate personal and business life.
6. Mapping your trade area with possible locations, the locations of competitors, and the locations of businesses that draw the same target customers can help you narrow your location options.

8.2 Obtain Space and Design the Physical Layout

7. To evaluate leases, compare the costs and expected benefits of various locations and the types of leases—gross, net, or percentage—offered. Calculating the rent per customer can help you determine which location is most cost effective.
8. The layout of a business depends on the type of business. For retail businesses, the aim of a layout is to attract and keep customers. For wholesale businesses, the aim of a layout is to store inventory in the most efficient manner. For manufacturing businesses, the aim of a layout is to facilitate the production process.

8.3 Purchase Equipment, Supplies, and Inventory

9. Once you determine your equipment and supply needs, you will need to identify and evaluate a number of vendors by obtaining quotes and asking about quality, financing terms, quantity discounts, and shipping and handling charges.
10. To determine the amount of inventory to keep in stock and the reorder point, consider the amount of expected sales, the time it takes your supplier to get merchandise to you, and how important it is for you not to be out of stock for the item.

What do you know now?

Read Ideas in Action on page 209 again. Then answer the questions a second time. How have your responses changed?

VOCABULARY BUILDER

Match each statement with the term that best defines it. Some terms may not be used.

1. A section of land that is zoned for industrial businesses only
2. Companies that sell products and services to businesses
3. The area from which a business expects to attract customers
4. An estimate for how much you will pay for merchandise or services
5. The person who owns and rents out buildings or space
6. A lease in which the tenant pays rent each month for the space occupied, and the landlord covers all property expenses for that space
7. A lease in which the landlord pays building insurance, and the tenant pays rent, taxes, and any other expenses
8. Areas that suffer from lack of employment opportunities
9. The person who pays rent to occupy space owned by someone else
10. A predetermined level of inventory that signals when new stock should be ordered

- a. enterprise zones
- b. gross lease
- c. industrial park
- d. inventory
- e. landlord
- f. net lease
- g. percentage lease
- h. quote
- i. reorder point
- j. tenant
- k. trade area
- l. vendors

REVIEW YOUR KNOWLEDGE

11. Which of the following is *not* a location option for a retail business?
 - a. downtown area
 - b. industrial park
 - c. community shopping center
 - d. warehouse
12. Which of the following service businesses would consider the same location factors as a retail business?
 - a. exterminating company
 - b. lawn service
 - c. hair salon
 - d. on-site computer repair service
13. Which of the following is *not* a good reason to locate a business in the home?

a. cost savings	c. limited space
b. more freedom	d. convenience
14. **True or False?** Availability of parking would be an important consideration for the location of a coffee shop.
15. **True or False?** Most entrepreneurs start out by purchasing the site where their business will be located.
16. In which type of lease does a landlord receive a portion of the tenant's revenue each month in addition to a base rent?
 - a. gross lease
 - b. net lease
 - c. percentage lease
 - d. tenant-landlord lease

17. Which of the following is the *least* important consideration when organizing the layout of a retail business?
 - a. lighting
 - b. window displays
 - c. aisle space
 - d. organization of supplies
18. Which of the following is the *least* important consideration for the layout of a manufacturing business?
 - a. organization
 - b. efficiency of workflow
 - c. safety
 - d. attractiveness
19. **True or False?** When purchasing supplies, equipment, and inventory, it is always best to purchase from the lowest-cost vendor.
20. Which of the following is *not* considered inventory?
 - a. dolls for a toy store
 - b. component parts of a product
 - c. vacuum cleaners owned by a maid service
 - d. all of the above are considered inventory
21. Which of the following is the *least* important factor in determining the reorder point for a sale item in your store?
 - a. the size of the item
 - b. the time it takes to receive merchandise from your supplier
 - c. how many units you sell each month
 - d. how important it is to you to not run out of stock

APPLY WHAT YOU LEARNED

22. You are planning to open a card and gift shop. Identify the trade area. What types of locations are available in your community? List the advantages and disadvantages of each. Are there competing card and/or gift shops in any of these locations? Are there other businesses that do not compete directly but attract the same kind of customer? What are these businesses? Why do you think these businesses chose this particular location?
23. You are going to open a gift shop that offers photo gifts such as photo keychains and mugs. You will take the photos yourself and assemble the products. Consider all of the location options for your business: downtown, shopping centers, stand-alone store, or a warehouse. Where would you locate your business and why?

MAKE ACADEMIC CONNECTIONS

24. **RESEARCH** Interview the owners or managers of three to five local businesses. What does each of these business owners see as advantages and disadvantages of their locations? Are these businesses successful?
25. **COMMUNICATION** Design the layout of a fitness club. Create a scale drawing of the space and show the placement of all of the equipment. You may want to use pictures from catalogs or magazines to show the type of equipment you have selected. Present your plan to the class and explain why you think your layout will make your business successful.
26. **MATH** You are choosing between a neighborhood shopping center and a stand-alone store for your shoe store. The monthly

rent for the shopping center is \$3,200; the monthly rent for the stand-alone location is \$2,500. The projected monthly customer traffic at the shopping center is 6,500 and the projected monthly traffic at the stand-alone location is 5,100. Which location will you choose and why? What other factors might you consider before choosing a location?

WHAT WOULD YOU DO?



You are looking for a vendor to supply your new business with a computer, a printer, and a copy machine. You have contacted several vendors for quotes. One of the vendors recently contacted you to offer you a “special” deal, but you had to agree to it before the end of the day. In addition to a competitive price for the equipment, he is offering you tickets to an NFL game in a private stadium suite. He wants you to agree to the deal without signing a contract and has asked that you pay him in cash. What would you do?

BUILD YOUR Business Plan *Project*

This activity will help you choose a location and vendors for your business idea.

1. Choose the location area that is best for your business. Why is it the best choice? Record your reasons on paper.
2. Using a local map, mark the trade area for your business. Mark the possible locations for your business and the locations of your competitors. Are there any businesses in the trade area that do not directly compete but attract a similar type of customer? If so, mark those on the map. For each area, write an evaluation that outlines why this would or would not be a good location for your business.
3. Determine if it will be more cost-effective for you to buy or lease space or to run your business from home. Consider rent-per-customer projections. Write a short paper justifying your decision.
4. Design the physical layout of your business. Create a scale drawing of the space and show the placement of all of the furniture, fixtures, and equipment. Indicate the planned use of each area. How does this layout meet your goals? Calculate the square footage requirements for the entire layout.
5. Make a list of the equipment and supplies you will need to start your business. Using the telephone book, trade magazines, the Internet, and other sources, locate five vendors. Contact the vendors to obtain information about their products, pricing, financial terms, and quantity discounts. Using the prices from each vendor, calculate the total cost of all equipment and supplies you will need. How do the vendors compare? Which one will you select? Why?

Planning a Career in Architecture and Construction



"My uncle is visiting from out West. He is excited about the solar panels he recently installed at his home. His city provided a \$1,000 rebate for solar panel installation. To obtain the rebate, the panels need to annually displace 1,500 kilowatt hours of grid-based power. My uncle's utility bills have gone down. He also feels good about doing his part to improve the environment by decreasing his dependence on the grid."

How do individuals and organizations transition their energy resources from traditional sources to environmentally friendly, renewable sources?

Solar power is a renewable energy source that is rapidly increasing in popularity. Many companies are available to guide individuals and corporations in utilizing solar energy and to assist in solar panel installation.

EMPLOYMENT OUTLOOK

- Solar energy consumption is expected to grow as part of the overall growth of U.S. energy consumption.
- Workers who are trained to participate in alternative energy sources may experience good job prospects.
- Individuals with college coursework in high-end technology will have the best opportunities in the utilities industry.

JOB TITLES

- Solar Installer
- Consultant, Solar Energy
- Solar Energy Project Manager
- Photovoltaic Lighting Designer
- Solar System Design Engineer

NEEDED SKILLS

- A Bachelor's Degree in Science, with an engineering major, is required for higher-level design, production, and management jobs.
- Expertise in a variety of areas including journeyman-level electrical knowledge, plumbing, and mount racking systems is needed for solar panel installers.

What's it like to work in Architecture and Construction

Paige, a solar panel installation contractor, has obtained installation contracts from a variety of companies. The companies that contracted for Paige's services provide their clients with on-site consulting, ranging from determining the optimal location of solar panels, to the filing of paperwork for government-based rebate and tax credit programs, to providing a six-month follow-up visit to ensure proper functioning of panels.

As Paige has been installing panels for many years, her experience is broad-based. Given the breadth of her experience, she can install panels at residential, commercial, or industrial sites.

Paige is planning to attend a conference that will focus on state and federal solar energy incentive programs. Becoming more knowledgeable about these issues is part of Paige's continuing education plan to prepare her to start her own solar energy consulting business.

What about you? Would you like to help clean up the environment by actively converting energy consumers to renewable, "green" energy sources?



BUYING AND MERCHANDISING MANAGEMENT TEAM DECISION MAKING EVENT

Your team is in charge of buying merchandise and clothing bearing the university's name, logo, and trademark for a large university bookstore on a campus that has 54,000 students. The university has a highly successful football and baseball team, attracting numerous fans to the campus on game days. Your team must understand product mix, product life cycles, seasonal markdown schedules, pricing strategies, target markets, and special promotional events. You will meet with the bookstore managers to explain your proposed product mix, markdown schedule for seasonal merchandise, and special sales events to sell merchandise. Your merchandising strategy must consider the fluctuating student population during the year. You must also explain a strategy to increase Internet merchandise sales.

Your team has 30 minutes to study a business situation and organize your analysis, using a management decision-making format. Participants have ten minutes to describe the team's analysis of the situation. The judge has five minutes to ask questions about the presentation.

PERFORMANCE INDICATORS EVALUATED

- Identify product opportunities.
- Describe the use of technology in the selling function.
- Explain the nature and scope of the product/service management function.
- Identify the impact of product life cycles on marketing decisions.
- Develop strategies to position the product/business.
- Identify products to fill customer needs.
- Explain the nature of sales management.

Go to the DECA web site for more detailed information.

Think Critically

1. Why must the clothing at the bookstore be unique from clothing carried in department stores and other retail outlets?
2. Why are scheduled merchandise markdowns important for retailers?
3. What types of special promotions could increase sales from fans and alumni attending football and baseball games?
4. Why should the bookstore consider Internet merchandise sales?

www.deca.org

Chapter 9

© PhotoDisc/Getty Images



Plan and Track Your Finances

9.1 Finance Your Business

9.2 Pro Forma Financial Statements

9.3 Recordkeeping for Businesses

school.cengage.com/entrepreneur/ideas

IDEAS IN ACTION

Electronic Safekeeping

Members of Generation Y, more so than previous generations, are increasingly reliant on the daily use of portable electronics. When Katelin Shea began her freshman year at New York University, she had her new laptop in tow. She needed a carrying case that would both fit her personal style and protect her expensive gadget from drops, bumps, and scratches. After an extensive search, she came up empty handed and decided to create a custom carrying case of her own. Using her mother's sewing machine and materials from a local craft store, she made her first colorful, custom-sized, protective sleeve. Before long, friends and family were offering to pay for cases of their own. From this, GadgetSleeves was born! Today, GadgetSleeves designs and produces functional, stylish, and fun protective sleeves for laptops, iPods, cell phones, cameras, and more.



© Katelin Shea

Katelin Shea, Owner/Founder of GadgetSleeves

Katelin did not start out with a formal business plan, but she wrote one out a few months later when taking an Entrepreneurship course. She entered her plan in the 2006 DollarDiva Business Plan Competition hosted by Independent Means, Inc., and she won! She has found that the research, statistics, and ideas she put into the plan have been extremely helpful to her as she runs GadgetSleeves.

Working from home, Katelin started GadgetSleeves with \$750 from her own savings. She used \$150 to buy a new sewing machine, \$200 for her first order of materials, and \$50 for promotional items. Later, she paid a tech-savvy classmate \$350 to create her web site.

Katelin encourages other aspiring entrepreneurs to use the Internet to its full advantage. Researching competitors, negotiating with suppliers, and even shipping products is much easier with the use of the Internet. Katelin also advises others not to go into business just to make money. "Although financial rewards are nice, you should go into business to solve a problem, fill a gap in the market, or expand on a hobby. If you do what you love and you do it well, the money will follow."

What do you know?

1. Can you think of a need that you have that is not being met? What could you do to meet that need?
2. If Katelin had not had the money she needed to start her business, what do you think she could have done?
3. Why do you think a web site opens up options for a business?

9.1

Finance Your Business

Goals

- Estimate your startup costs and personal net worth.
- Identify sources of equity capital for your business.
- Identify sources of debt capital for your business.

Terms

- net worth
- debt-to-equity ratio
- equity capital
- venture capitalists
- debt capital
- collateral

Focus on Small Business

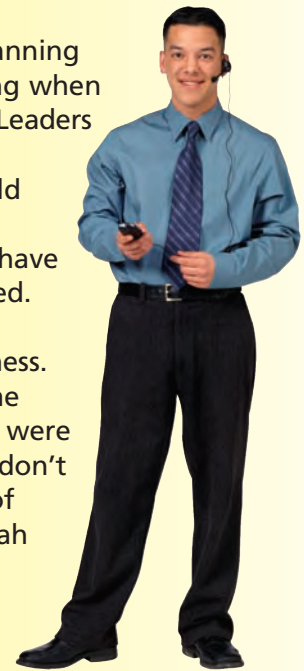
Line up your financing

Monty was excited about starting his own meeting planning business. He had learned much about meeting planning when serving as a state officer for his state's Future Business Leaders of America chapter. He couldn't wait to get started.

Monty started a list of all the things that he would need to buy for his business. He realized that he was going to need some financial assistance as he did not have enough money saved to purchase everything he needed. He called his friend Sarah for some advice.

"Sarah, I need some help financing my new business. Who do you think I should ask?" Sarah had taken some business courses in school and remembered that there were many different avenues for funding a business. "Why don't you start with your friends and family and see if any of them are interested in investing in your business," Sarah suggested. "If not, I've got lots more ideas!"

Work as a Team Do you think your friends and family members would be willing to loan money or invest in your business? If not, who else could you approach for funding?



© PhotoDisc/Getty Images

Determine if you need financial assistance.

Assess Your Financial Needs

As you start a business, you will have many decisions to make regarding its financing. Your financial needs will vary depending on the size and type of business you start. If you are starting a very small business, you may be able to provide all the startup money you will need. If your business will be large or require special equipment, you may need to look to others for help raising the startup money.

Before you can approach a lender or investor about financing your business, you will have to prepare some financial documents. To begin, you should estimate your startup costs and create a personal financial statement. Then you will prepare pro forma financial statements of the cash flow statement, income statement, and balance sheet.

Financial statements based on projections are known as *pro forma financial statements*. You will learn more about pro forma financial statements in the next lesson. These items allow potential lenders and investors to determine if your business is viable. They also help lenders decide whether the financing you are requesting is reasonable.

Startup Costs

Itemizing your startup costs is an important part of determining how much money you need to start your business. You will want to be sure you have accounted for all of the items you will need. Common startup items to be purchased include the following:

- Equipment and supplies, such as computers, telephones, and fax machines
- Furniture and fixtures, such as desks and chairs
- Vehicles, such as delivery trucks
- Remodeling, such as electrical and plumbing expenses
- Legal and accounting fees
- Licensing fees

Felicia Walters plans to start a lighting fixture store. To help her determine how much money she will need to borrow, she calculates her startup costs. She must include her estimate of startup costs with the other documents she provides to lenders.

Personal Financial Statement

In order to determine if you have the resources you need to finance your business, begin by assessing your net worth. **Net worth** is the difference in what you own, called *assets*, and what you owe, called *liabilities*. Net worth is also referred to as *equity*. To calculate your net worth, you should prepare a *personal financial statement*. On the left side, list all of your assets with their value. Include cash, investments, and any property. Total the worth of these items. On the right side, list your liabilities and total the amount that you owe. Then subtract your total liabilities from your total assets to determine your net worth.

Felicia Walters prepares a personal financial statement to help her determine whether she is able to finance her new business. She finds that her net worth is \$27,800 as shown on the next page. After comparing her startup costs to her net worth, Felicia determines that she will need to seek additional financial resources for her business. Felicia will share her personal financial statement and startup cost estimates with potential lenders and investors when she seeks financing for her business.

★ Develop Your Reading Skills

As you read this chapter, list all of the key terms. Then write a sentence using the key term to demonstrate comprehension of the term.

STARTUP COSTS Walters Electric	
Item	Estimated Cost
Equipment and supplies	
Computers (3 @ \$1,500)	\$ 4,500
Scanner	175
Cash registers (2 @ \$1,800)	3,600
Fax machine	400
Supplies	300
Subtotal	<u>\$ 8,975</u>
Furniture and fixtures	
Desks (4 @ \$400)	\$ 1,600
Chairs (8 @ \$75)	600
Subtotal	<u>\$ 2,200</u>
Vehicles	
Delivery truck	\$10,000
Automobile	8,000
Subtotal	<u>\$18,000</u>
Remodeling	
Drywall replacement	\$ 1,000
Electrical work	2,500
Paint	1,000
Carpet	3,000
Subtotal	<u>\$ 7,500</u>
Legal and accounting fees	<u>\$ 3,000</u>
Total	<u>\$39,675</u>



PERSONAL FINANCIAL STATEMENT			
Felicia Walters			
Assets		Liabilities	
Cash	\$ 5,000	Car loan	\$ 6,900
Checking account	13,500	College loan	4,000
Certificate of Deposit	6,000	Credit cards	1,300
Stock	10,000		
Computer equipment	3,000		
Coin collection	2,500		
Total assets	\$40,000	Total liabilities	\$12,200
Total assets – Total liabilities = Net worth			
\$40,000 – \$12,200 = \$27,800			

Checkpoint

Why is the net worth of an entrepreneur important to potential investors in the business?

Equity Capital

There are two types of financing available for your business—equity and debt financing. You must consider your company's **debt-to-equity ratio**, or the relation between the dollars you have borrowed and the dollars you have invested in your business. Lenders and investors look at this ratio to assess risk. The higher percentage of your own money that you have invested, the easier it will be for you to get others to invest.

If your company has a low ratio of debt to equity, you should probably look for debt financing. If your company has a high ratio of debt to equity, you should work to increase equity in your business. Having the right mix of debt and equity will help ensure your business's sound financial future.

Equity capital is money invested in a business in return for a share in the profits of the business. Entrepreneurs may seek equity capital when they do not qualify for other types of financing and are not able to fully finance their businesses out of their own savings. Equity capital can also supplement other money that is borrowed. You may provide much of the equity for your business yourself. You may also obtain equity through people you know or through venture capitalists.

Personal Contributions

Many entrepreneurs use their personal savings to finance the start of their businesses. Investing personal finances can help you get a loan from a bank. By investing your own money, you demonstrate to the bank that you have faith that your business will succeed.

Friends and Relatives

Friends and relatives can be a good source of equity capital. They will already be familiar with your business idea and know whether you are trustworthy and a good risk. They may be willing to invest more money in your business than other sources in return for a share of the business profits.



© PhotoDisc/Getty Images

What are the pros and cons of borrowing money from family and friends?

Venture Capitalists

Some privately owned companies get financing through venture capitalists. **Venture capitalists** are individuals or companies that make a living investing in startup companies. They carefully research opportunities that they believe will make above-average profits. They are usually interested in companies that have the potential of earning hundreds of millions of dollars within a few years. The prospect of a company going public by publicly offering shares of stock for sale also attracts venture capitalists. Because of the desired criteria, many small businesses would have trouble attracting the interest of venture capitalists.

Checkpoint

What are some of the ways entrepreneurs can get equity capital?

Debt Capital

Debt capital is money loaned to a business with the understanding that the money will be repaid, usually with interest. You can borrow money from friends, relatives, and banks. Bank loans may be secured or unsecured.

Friends and Relatives

If friends and relatives are not interested in investing in your business with equity capital, they may be willing to loan you money. Before borrowing from friends or relatives, consider how the loan may affect your relationship with them. Those who loan you money might also feel that they can give you advice along with their money. Since you are using their money, they might not understand if you do not take their advice. You may decide that the risk of losing a friend if you are unable to pay back the borrowed funds is not worth taking.

If you take a loan from friends or relatives, you should prepare a formal agreement that spells out the terms of the loan. You and everyone



involved in the loan should sign the agreement. Be sure both you and the individuals loaning the money understand exactly how much interest and principal you will pay each month. Also specify what your obligations are to pay back the loan if your business is not successful.

Commercial Bank Loans

Most businesses take out loans from banks. Entrepreneurs usually have an established relationship with a bank and begin looking for funds there. When a loan is taken out, it must be repaid with interest in a certain time period. There are different types of loans that banks offer their customers.



© PhotoDisc/Getty Images

What kinds of information might be requested on a loan application?

SECURED LOANS Loans that are backed by collateral are called *secured loans*. **Collateral** is property that the borrower forfeits if he or she defaults on the loan. Banks demand collateral so that they have some recourse if the borrower fails to repay the loan.

Suppose you take out a \$25,000 business loan and use your home as collateral. If you fail to repay the loan, the bank has the right to take ownership of your home and sell it to collect the money you owe. Banks accept different forms of collateral, including real estate, savings accounts, life insurance policies, stocks, and bonds.

Types of secured loans include the following:

1. **Line of credit** An agreement by a bank to lend up to a certain amount of money whenever the borrower needs it is called a *line of credit*. Banks will charge a fee for this program whether or not money is actually borrowed. In addition, they will charge interest on the borrowed funds. Most businesses establish lines of credit so that funds are readily available to help them make purchases when necessary.
2. **Long-term loan** A loan payable over a period longer than a year is a *long-term loan*. Long-term loans are generally made to help a business make improvements that will boost profits. Nicole Brenner, owner of a small neighborhood coffee shop, took out a \$50,000, five-year loan so that she could increase the size of her shop. She will repay the loan with the extra money she will earn by serving more customers in her expanded dining room.
3. **Accounts receivable financing** Many businesses allow their customers to charge merchandise and services and pay later. The customers' owed balances are called the business's *accounts receivable*. A bank will loan a business up to 85 percent of the total value of its accounts receivable if it feels that the business's customers are

good credit risks. As the receivables are paid, the payments are forwarded to the bank. The interest rate for accounts receivable financing is often higher than for other types of loans.

4. **Inventory financing** When banks use the inventory held by a business as collateral for a loan, it is called *inventory financing*. Banks usually require that the value of the inventory be at least double the amount of the loan, and the business must have already paid its vendors for the inventory in full. Banks are often not eager to make this kind of loan. If the business defaults, the bank ends up with inventory it may have trouble reselling.

UNSECURED LOANS Loans that are not guaranteed with collateral are unsecured loans. These loans are made only to the bank's most creditworthy customers. Unsecured loans are usually made for very specific purposes. They are usually short-term loans that have to be repaid within a year. A business may obtain a short-term loan to help with temporary cash flow problems during slow or seasonal periods. Unsecured lines of credit are also available for those who have good credit.

REASONS A BANK MAY NOT LEND MONEY Banks use various guidelines to determine whether borrowers are a good risk. They reject applications that do not meet their criteria. Some of the main reasons banks turn down loan applicants include the following:

1. **The business is a startup.** Banks are often reluctant to lend money to startup businesses because new businesses have no record of

Famous Entrepreneur

The Wright Brothers

When you think of the Wright Brothers, you probably think of them as the first men to fly. But before they were flying a plane at Kitty Hawk, they were entrepreneurs in Dayton, Ohio. As children, Wilbur and Orville loved fixing and experimenting with machines. They sold kites to other children in their neighborhood for extra money. Wilbur invented a machine to fold papers for mailing when he was a teenager. Orville and a friend set up a small printing firm when Orville was 14 years old. Orville and Wilbur went on to publish their own newspaper, *West Side News*, in 1889. Cycling was a growing sport at that time. Because of their ability to repair things, people were always

asking the Wrights to repair their bicycles. So in their early twenties, Wilbur and Orville opened the Wright Cycle Company. Using the profits from their bicycle shop, they began to study flight and experiment with gliders and kites. These experiments led them to the powered flying machine they flew successfully on December 17, 1903.

Think Critically

Do you think Wilbur and Orville would have been able to finance their flight experiments if they had not had income from their own business?



Why do entrepreneurs often have more than one business venture?

repaying loans. They are more likely to default on their loans than established companies.

2. **Lack of a solid business plan.** Banks evaluate businesses based on their business plans. A company with a poorly written or poorly conceived business plan will not be able to obtain financing from a bank.
3. **Lack of adequate experience.** Banks want to be sure that the people setting up or running a business know what they are doing. You will have to show that you are familiar with the industry and have the management experience to run your own business.
4. **Lack of confidence in the borrower.** Even if your business plan looks solid and you have adequate experience, you may fail to qualify for financing if you make a bad impression on your banker. Make sure you dress and behave professionally. Show up on time for appointments, and provide all information your banker requests.
5. **Inadequate investment in the business.** Banks are suspicious of entrepreneurs who do not invest their own money in their businesses. You will have to commit a significant amount of your own money if you are to receive financing from a bank.

Obtaining bank financing for a startup business is difficult but not impossible if you can show that you are confident, well prepared, and able to repay the loan. Being aware of banks' most common objections can help you prepare for the application process. For instance, you can properly prepare your business plan, wear a business suit to bank appointments, and arrive on time to make a good impression.

Other Sources of Loans

In addition to commercial banks, there are many government agencies that can assist you with debt capital loans.

1. **Small Business Administration** The SBA aids about 1 million entrepreneurs every year, most often by guaranteeing loans made by commercial banks. This means if you default on the loan, the SBA will pay a certain percentage of the loan to the bank. This helps banks feel more comfortable about lending money. The SBA

also makes funds available to non-profit organizations that, in turn, make loans to eligible borrowers.

2. **Small Business Investment Companies** SBICs are licensed by the SBA to make loans to and invest capital with entrepreneurs.
3. **Minority Enterprise Small Business Investment Companies** MESBICs are special kinds of SBICs that lend money to small businesses owned by members of ethnic minorities.
4. **Department of Housing and Urban Development** HUD provides grants to cities to help improve impoverished areas. Cities use these grants to make loans to

NETBookmark

The Small Business Administration (SBA) offers many loan programs to assist small businesses. Its programs offer many benefits, such as longer payment terms and larger loan amounts than might be available through a conventional commercial bank loan. Access school.cengage.com/entrepreneur/ideas and click on the link for Chapter 9. Read about the various SBA loan programs and describe three of them.

school.cengage.com/entrepreneur/ideas

private developers who must use the loans to finance projects in needy areas.

5. **The Economic Development Administration** The EDA is a division of the U.S. Department of Commerce that lends money to businesses that operate in and benefit economically distressed parts of the country. Borrowing from the EDA is similar to borrowing from the SBA, but the application is more complicated and the restrictions are tighter.
6. **State Governments** Government assistance may also be available at the state level. Almost all states have economic development agencies and finance authorities that make or guarantee loans to small businesses.
7. **Local and Municipal Governments** City, county, or municipal governments sometimes make loans to local businesses. The loans are usually small—\$10,000 or less.

did you KNOW?

The SBA is the largest single financial backer for the nation's small businesses. It has a portfolio of business loans, loan guarantees, and disaster loans worth more than \$45 billion, in addition to a venture capital portfolio of \$13 billion.

Checkpoint

Where can entrepreneurs look for debt financing?

9.1 Assessment

THINK ABOUT IT

1. What are some of the challenges you might encounter if you get equity financing from friends and/or family members?
2. Why is a secured loan easier to get than an unsecured loan?
3. Why would a bank be more willing to grant an SBA-guaranteed loan to a new business owner?

MAKE ACADEMIC CONNECTIONS

4. **MATH** Tisha Appleton obtained an SBA-guaranteed loan from her bank for \$45,000 for her new business. The SBA guaranteed 75 percent of the loan. How much has the bank risked losing if Tisha's business fails?
5. **COMMUNICATION** When applying for a loan, most lenders will want to see a personal financial statement. Using the Activity CD, open the activity "Personal Financial Statement." Print a copy and complete the personal financial statement required by the SBA.



TEAMWORK

Work in small groups. You want to start a home remodeling business. You need money to purchase remodeling equipment and a new truck. Identify sources of financing for the business. Role play a scenario in which you are meeting with a potential investor. Explain your business idea and your need for funds, and make a request for funding.



9.2

Pro Forma Financial Statements

Goals

- Prepare a pro forma cash flow statement.
- Prepare a pro forma income statement.
- Prepare pro forma balance sheet.

Terms

- cash flow statement
- income statement
- balance sheet

Focus on Small Business

Show me the money!

"So, Monty," asked Sarah, "how much money do you think your business will make?" "And I'm supposed to know that how?" Monty replied. "Well, take a look at your pro forma financial statements," Sarah answered.

"Well, Sarah, once again you are showing me how much I don't know!"

"Boy, you'd be in a mess if I wasn't your friend," Sarah responded.

"There are financial statements you should prepare to help you estimate the finances of your business. The pro forma income statement estimates how much money will come in, how much you will spend, and the amount of any projected profit or loss. Some people even call it a profit/loss statement."

"Wow, it sounds like a pro forma income statement would be helpful in trying to obtain a loan," Monty replied. "What other financial statements do I need?"

"Come on, Monty, we've got work to do. There's also a pro forma cash flow statement and balance sheet. Let's get started!"

Work as a Team Discuss the reasons you think it is important to prepare pro forma financial statements. What types of information do you think that a business owner can get from these financial statements? Why do you think pro forma financial statements should be included as part of a business plan?



Financial statements show how well your business is doing.

© Getty Images/PhotoDisc

Cash Flow Statement

Financial statements are important when you are trying to raise capital for your business. The financial statements you prepare for your business plan are pro forma financial statements and are based on projections. The cash flow statement, income statement, and balance sheet all tell you something different about the condition of your business.

For many, the cash flow statement is the most important financial statement. A **cash flow statement** is an accounting report that describes

the way cash flows into and out of your business over a period of time. Because it deals with actual cash coming in and going out of a business, it shows how much money you have available to pay your bills.

Forecast Receipts and Disbursements

To create a pro forma cash flow statement, you will need to estimate your monthly cash receipts and monthly cash disbursements. Cash receipts include cash sales, collected account receivables, tax refunds, and funds from bank loans and investors. When you forecast the amount of your cash receipts, you need to analyze the demand for each of your products and services. You also need to know the price you will charge for each item.

Felicia Walters estimates her total cash sales by multiplying the quantity of each type of product she expects to sell by the price she has set for each item. In addition, Felicia estimates her other monthly cash receipts as shown below.

FORECASTED RECEIPTS			
Walters Electric			
January 20—			
Cash sales	Quantity Sold	Price	Total
CFL bulbs	20	\$ 15	\$ 300
Indoor light fixtures	10	155	1,550
Outdoor lights	6	175	1,050
Subtotal			<u>\$2,900</u>
Accounts receivable			<u>\$ 300</u>
Bank loan			<u>\$1,000</u>
Total			<u><u>\$4,200</u></u>

Cash disbursements may include payments for cost of goods (what you pay manufacturers or wholesalers to get products and services to sell), accounts payable (credit accounts with suppliers), rent, salaries, taxes, office supplies, utilities, insurance, advertising, loans, and other expenses. Felicia's estimated monthly cash disbursements are shown in the table to the right.

Prepare the Cash Flow Statement

After making projections of cash receipts and cash disbursements, you are ready to prepare your cash flow statement. You should create monthly pro forma cash flow statements for the first year of operation and annual statements for the second and third years to give your lender an accurate picture of your cash flow over time.

Net cash flow is the difference between cash receipts and disbursements.

Cash receipts – Cash disbursements = Net cash flow

FORECASTED DISBURSEMENTS	
Walters Electric	
January 20—	
Disbursement	Amount
Cost of goods	\$2,400
Rent	900
Utilities	100
Salaries	2,000
Advertising	700
Supplies	100
Insurance	75
Payroll taxes	175
Other	50
Total	<u><u>\$6,500</u></u>



PRO FORMA CASH FLOW STATEMENT Walters Electric January–June 20—						
	Jan	Feb	Mar	Apr	May	June
Cash receipts	<u>\$4,200</u>	<u>\$5,410</u>	<u>\$5,750</u>	<u>\$6,320</u>	<u>\$7,375</u>	<u>\$8,130</u>
Cash disbursements						
Cost of goods	\$2,400	\$2,520	2,520	2,640	3,300	3,480
Rent	900	900	900	900	900	900
Utilities	100	100	100	100	100	100
Salaries	2,000	2,000	2,000	2,000	2,000	2,000
Advertising	700	700	700	700	700	700
Supplies	100	115	130	150	150	150
Insurance	75	75	75	75	75	75
Payroll taxes	175	175	175	175	175	175
Other	50	50	50	50	50	50
Total disbursements	<u>\$6,500</u>	<u>\$6,635</u>	<u>\$6,650</u>	<u>\$6,790</u>	<u>\$7,450</u>	<u>\$7,630</u>
Cash Flow	<u>–\$2,300</u>	<u>–\$1,225</u>	<u>–\$ 900</u>	<u>–\$ 470</u>	<u>–\$ 75</u>	<u>\$ 500</u>

If cash receipts total more than disbursements, your business has a positive cash flow. You can put this money in the bank, pay down debt, or use it to expand your business. If disbursements total more than cash receipts, your business has a negative cash flow. You may have to borrow money or ask your creditors to give you more time to pay. Preparing pro forma statements helps you to anticipate when negative cash flows will occur, so you can plan for how you will handle or avoid them. Felicia Walter's pro forma cash flow statement is shown above.

Many entrepreneurs create two types of cash flow statements based on a worst-case scenario and a best-case scenario. For a worst-case scenario, you should project lower cash receipts and higher cash disbursements than you think you will have. For a best-case scenario, you should project the highest cash receipts and lowest cash disbursements your business is likely to have.

Economic Effects on Cash Flow

Changes in the economy can have a dramatic effect on the cash flow of a business. During the good economic times of the 1990s, many businesses saw large amounts of cash flowing into their companies and experienced positive cash flows. However, the economic slow-down that resulted after September 11, 2001, caused many businesses to experience unexpected negative cash flows. When making projections, business owners should look at economic forecasts and make conservative estimates. Remembering that changing economic conditions can affect cash flows, it is best to err on the side of caution.

Checkpoint

What does a cash flow statement show?

Income Statement

An **income statement** shows the business's revenues and expenses incurred over a period of time and the resulting profit or loss. For this reason, it is sometimes called the *profit/loss statement*. An income statement can help you do the following:

1. Examine how sales, expenses, and income are changing over time.
2. Forecast how well your business can expect to perform in the future.
3. Analyze your costs to determine where you may need to cut back.
4. Identify categories of expenditures you may want to increase or decrease, such as advertising.

While the cash flow statement deals with actual cash coming in and going out, the income statement shows revenues that you have not yet received and expenses that you have not yet paid.

Suppose Walters Electric sells \$5,000 worth of lighting in June. The company's monthly income statement would show income of \$5,000. Felicia may not actually have received \$5,000, because some customers may have paid on credit. They will not make payments until July or August. Further, some credit customers may fail to ever pay their bills.

Customers are not the only people who defer payments. Felicia may purchase \$1,500 worth of merchandise to sell but wait 30 days to pay the invoice. Because no cash has been paid for this purchase, it will not appear on the cash flow statement. In contrast, the income statement will show that Felicia incurred an expense of \$1,500.

Prepare a Pro Forma Income Statement

Preparing a pro forma income statement for a number of years will help lenders see the long-term growth of your business. The pro forma income statement consists of the following parts:



Why should a business estimate the amount of revenue it expects to earn?



PRO FORMA INCOME STATEMENT

Walters Electric, 20—

	Year 2	Year 3
Revenue	\$115,000	\$125,000
Cost of goods sold	55,400	60,000
Gross profit	\$ 59,600	\$ 65,000
Operating expenses		
Salaries	\$ 26,705	\$ 27,315
Rent	10,800	10,800
Utilities	1,230	1,260
Advertising	1,200	1,200
Insurance	900	900
Supplies	600	615
Other	615	615
Total operating expenses	\$ 42,050	\$ 42,705
Net income before taxes	\$ 17,550	\$ 22,295
Taxes	7,020	8,918
Net income/loss after taxes	\$ 10,530	\$ 13,377

- **Revenue** The dollar value of the goods or services a business sells to customers is called revenue.
- **Cost of goods sold** The cost of the inventory a business sells during a particular period is called cost of goods sold. Only businesses that have inventory will have this item on their income statements. It is listed separately from the other expenses.
- **Gross profit** The difference between revenue and cost of goods sold is the gross profit.
- **Operating expenses** The expenses necessary to operate a business are the operating expenses. They include salaries, rent, utilities, advertising, insurance, supplies, and other expenses. All businesses pay operating expenses.
- **Net income before taxes** Net income before taxes is the amount remaining after cost of goods sold and operating expenses are subtracted from revenue. It shows how much you earned before taxes.
- **Taxes** Taxes are usually listed separately from other expenses.
- **Net income/loss after taxes** After taxes are subtracted, the result is the net income or loss for the period.

Checkpoint

What does an income statement show?

Balance Sheet

A **balance sheet** is a financial statement that lists what a business owns, what it owes, and how much it is worth at a particular point in time. It does so by identifying the assets, liabilities, and owner's equity of the business. It is based on the accounting equation:

$$\text{Assets} = \text{Liabilities} + \text{Owner's Equity}$$

Assets are items of value owned by a business. They include items such as cash, equipment, and inventory. Liabilities are amounts that a business owes to others. They include loans and outstanding invoices. Owner's equity is the amount remaining after the value of all liabilities is subtracted from the value of all assets. A business that has more assets than liabilities has positive net worth. A business that has more liabilities than assets has negative net worth.

Prepare a Pro Forma Balance Sheet

You must estimate the amount of assets, liabilities, uncollectible accounts, and asset depreciation when preparing a pro forma balance sheet for your business. Felicia Walters' pro forma balance sheet for her business is shown below.

TYPES OF ASSETS Businesses usually separate assets into fixed assets and current assets. *Fixed assets* are those that will be used for many years. They include buildings, furniture, and computers. *Current assets* are cash, other assets that can be converted into cash, and items that are used up in normal business operations. One asset that can be converted into cash is inventory. Assets that are used up in business operations are supplies. Another special type of current asset is accounts receivable. *Accounts receivable* are the amounts owed to a business by its credit customers. When they are collected, they are converted into cash.

TYPES OF LIABILITIES Businesses usually separate liabilities into long-term liabilities and current liabilities. *Long-term liabilities* are debts that are payable over a year or longer. A mortgage is a type of long-term liability. *Current liabilities* are debts that are due to be paid in full in less than a year. A special kind of current liability is accounts payable. *Accounts payable* are amounts owed to vendors for merchandise purchased on credit. Businesses can usually choose to pay later for merchandise they receive now. Because a business generally pays invoices from vendors within 30 to 90 days, accounts payable is a current liability.

ASSET REDUCTIONS Some customers will fail to pay for the merchandise they purchased on credit. The amount a company estimates it will

PRO FORMA BALANCE SHEET			
Walters Electric			
December 31, 20—			
Assets		Liabilities	
<i>Current assets</i>		<i>Current liabilities</i>	
Cash	\$ 1,000	Accounts payable	\$12,000
Accounts receivable	8,000		
Less allowance for uncollectible accts.	–500		
Inventory	14,000	<i>Long-term liabilities</i>	
Total current assets	<u>\$22,500</u>	Loans payable	<u>\$17,900</u>
<i>Fixed assets</i>		Total liabilities	<u>\$29,900</u>
Equipment	\$ 8,975		
Less depreciation	–1,795		
Furniture	2,200		
Less depreciation	–220		
Vehicles	18,000	Owner's Equity	
Less depreciation	–3,600	Felicia Walters	<u>\$16,160</u>
Total fixed assets	<u>\$23,560</u>	Total liabilities and owner's equity	
Total assets	<u>\$46,060</u>		<u>\$46,060</u>



not receive from customers is known as the *allowance for uncollectible accounts*. This amount should be subtracted from the assets.

Business equipment will lose value over time just as a car loses value as it gets older. The lowering of an asset's value to reflect its current worth is called *depreciation*. Estimates for uncollectible accounts and depreciation should be included to ensure that the balance sheet provides an accurate picture of the business's net worth.

Checkpoint

Name one example each of a current liability, a long-term liability, a current asset, and a fixed asset.

9.2 Assessment

THINK ABOUT IT

1. Why would you prepare both a best-case and a worst-case pro forma cash flow statement?
2. Green Golf Course has a positive cash flow only six months of the year. What should the owner do with the extra cash during these months?
3. When making financial projections, why must a business owner consider economic conditions?

MAKE ACADEMIC CONNECTIONS

4. **PROBLEM SOLVING** Create a pro forma cash flow statement to project your cash receipts and disbursements over the next six-month period. Do you project a positive cash flow? If not, how can you improve your cash flow?
5. **MATH** In May, Yoder's Bookstore had sales of \$5,000, cost of goods sold of \$3,000, operating expenses of \$800, and taxes of \$400. Calculate Yoder's gross profit and final net income or loss.
6. **MATH** At the end of its first year of operations, Berganstein Sportswear had current assets of \$13,000, fixed assets of \$25,000, current liabilities of \$7,000, and long-term liabilities of \$14,000. What is the amount of owner's equity?



TEAMWORK

Working in a small group, research the state of the U.S. economy today and future forecasts of the economy. Prepare a brief presentation to share what you have learned. Based on your findings, predict how today's economy could affect the cash flow of a new business. Then, based on future forecasts, predict how the economy will affect the cash flow of a business in coming years.

9.3

Recordkeeping for Businesses

Goals

- Describe the use of journals and ledgers in a recordkeeping system.
- Explain the importance of keeping accurate and up-to-date bank, payroll, and tax records.

Terms

- transaction
- journals
- account
- check register
- payroll

Focus on Small Business

Keeping it all straight

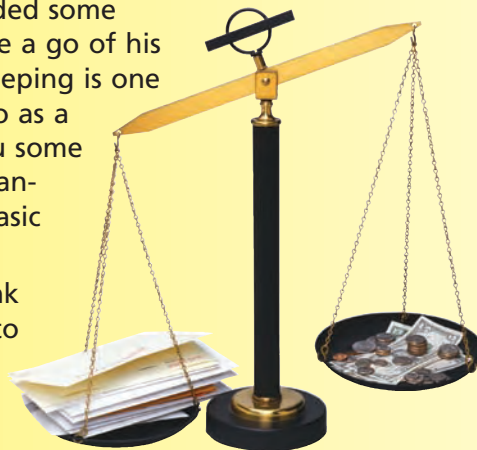
After securing financing for his business, Monty was ready to get started. He purchased all of his equipment and supplies, sent out some advertising fliers, and set up meetings with potential clients. Two months into his business, he was very surprised to find a notice from his bank informing him that he had written checks from a bank account that had no funds. "How did this happen?" he asked Sarah. "Did you reconcile your bank statement last month?" Sarah responded. "Reconcile what?" Monty replied.

"Oh, Monty, don't tell me you don't know how to reconcile your bank statement! But you do know how to journalize your transactions don't you?"

"Well, Sarah, I guess I wasn't as prepared as I thought. I have no idea what you are talking about!"

Sarah realized that Monty needed some serious help if he was going to make a go of his business. "Monty, financial recordkeeping is one of the most important things you do as a business owner. We need to get you some help from an accountant. In the meantime, I'll give you a few lessons in basic recordkeeping!"

Work as a Team Why do you think financial recordkeeping is essential to the success of a business? What types of records do you think business owners need to keep? What types of trouble could result from poor recordkeeping?



Good recordkeeping keeps everything in balance.

© PhotoDisc/Getty Images

Recording Transactions

A **transaction** is any business activity that changes assets, liabilities, or net worth. Accurate recordkeeping of your business transactions will help you keep track of how much money you have earned, how much you have spent, how much money you owe, and how much customers



© Digital Vision/Getty Images

Why is it important to keep track of business transactions?

owe you. It will also help you create financial statements to determine your business's net worth and how much profit you have made.

Journals

Journals are accounting records of the transactions you make. There are five different journals that businesses use to record their transactions.

1. **Sales journal** This is used to record only sales of merchandise on account. Merchandise sold on account means that customers receive goods or services now that they will pay for later.
2. **Cash payments journal** This is used to record only cash payment transactions. Any cash, check, or electronic payment a business makes is recorded in this journal.
3. **Cash receipts journal** This is used to record only cash receipt transactions. Cash sales and cash payments received from customers on their credit accounts are recorded in this journal.
4. **Purchases journal** This is used to record only purchases of merchandise on account. If you receive merchandise today but pay for it later, you should record this in the purchases journal.
5. **General journal** This is used to record any kind of transaction. Some businesses use only a general journal. Businesses that use the four special journals described above record transactions that do not fit in the other four journals in the general journal.

Ledgers

Businesses also use a general ledger that is made up of accounts. An **account** is an accounting record that provides financial detail for a particular business item, such as for cash, sales, rent, and utilities. The general ledger will have an account for every type of asset, liability, revenue, expense, and so forth. Transactions entered into the journals are posted, or transferred, to the general ledger accounts affected by the transactions. Posting is generally done every one to two days to

Business Records

Good recordkeeping can help you make smart business decisions. Incomplete or inaccurate records can cause you to mismanage your business or can cause serious legal problems. You will need to keep accurate banking, payroll, and tax records. These records may be kept manually or electronically.

Banking Records

You will need to open a checking account for your business. You will use your business account for all deposits and withdrawals related to your business. If you already have a personal checking account, you will still need a separate one for your business.

When you open your checking account, you will receive a set of checks and a check register. A **check register** is a booklet in which you record the dates and amounts of the checks as well as the names of people or businesses to whom you have written the checks. You can also maintain a check register electronically using computer software.

WHAT WENT WRONG ?

All Your Eggs in One Basket

After working for six years at a Toyota dealership, Billy Wong borrowed money from his family and started Japanese Car Parts Distributors (JCP). The business grew, and in ten years it had 12 employees, thousands of parts in inventory, and hundreds of customers across the country.

Billy kept handwritten records for the business. Before long, his 18-year-old, computer-whiz son, Tommy, wouldn't let him ignore the advantages of computerizing his recordkeeping. So Billy gave Tommy the task of setting up a computer system and transferring the accounts, inventory, and financial information from his paper records to the new electronic format. Within a year, Billy stopped keeping handwritten records in favor of Tommy's computerized system, and in the next year, the business ran more smoothly than ever.

Tragedy struck the business one December night when Tommy found robbers in the business office. Tommy was badly injured by the thieves and was rushed to the hospital. Sadly, he died on the way. If this wasn't enough for Billy to handle, the thieves also stole the office computer.

Billy had left all the electronic recordkeeping to his son, and he had no idea whether Tommy had made backup copies of all the files that had been stored on the stolen computer. Billy found that it would take months and a large amount of money to set up a new computerized recordkeeping system.

Think Critically

1. Was Billy wrong to trust his young son with so much responsibility?
2. Would JCP's problems have been solved if they had found the computer?



© PhotoDisc/Getty Images

Backing up computer files can prevent problems.



© PhotoDisc/Getty Images

How can you balance your checking account?

BALANCE YOUR ACCOUNT Every time you write a check or make a deposit, you should balance your check register. Balancing your check register is very important because it will prevent you from accidentally writing checks when you do not have enough money in your account to cover them. Writing bad checks is illegal! If your checks do not clear, your suppliers may stop shipping merchandise to you. Businesses and banks will charge you fees for having to deal with the bad checks.

RECONCILE YOUR ACCOUNT Every month you will receive a bank statement that shows all of your deposits, checks paid, and bank fees. When you receive your bank statement, you should *reconcile* the bank statement with your check register. The bank statement balance will not be the same as your check register balance because of checks that you have written that have not cleared the bank and deposits that you made after the bank statement was prepared.

The steps in reconciling your account are as follows:

1. Compare the bank statement with your check register. Place a checkmark in your check register by the checks that you have written that have cleared the bank. Also checkmark the deposits that you have made that have cleared the bank. Any remaining checks or deposits that are not listed on the bank statement are classified as *outstanding*.
2. Using the account reconciliation form on the back of your bank statement, enter the amount of your bank statement balance.
3. List outstanding deposits and add them to the bank statement balance.
4. List outstanding checks and deduct them from the bank statement balance.
5. Record the checkbook balance in the space provided.



6. If there were any deposits on your statement that you forgot to write in your check register, list them and add them to the checkbook balance.
7. Record any fees that the bank has charged your account and subtract them from the checkbook balance.
8. If your account earns interest from the bank, record the amount of interest earned and add it to the checkbook balance.
9. The bank statement balance and the checkbook balance should now be equal. Be sure to record any fees charged or interest earned in your checkbook. If your balances do not match, double check your math first. Then review your records to see if all checks and deposits have been recorded in your checkbook and processed by the bank correctly.

BANK RECONCILIATION			
Bank statement balance	\$2,151.00	Balance from checkbook	\$2,501.15
Add outstanding deposits	<u>660.00</u>	Add deposit not recorded	<u>0.00</u>
Subtotal	\$2,811.00	Subtotal	\$2,501.15
Deduct outstanding checks:		Deduct bank fees	<u>12.00</u>
#345 \$ 60.00		Balance less fees	\$2,489.15
#366 105.60			
#369 <u>150.00</u>		Add interest earned	<u>6.25</u>
Total outstanding checks	<u>315.60</u>		
Adjusted bank balance	<u>\$2,495.40</u>	Adjusted checkbook balance	<u>\$2,495.40</u>

Payroll Records

If you have employees working for you, you will have to maintain payroll records. A **payroll** is a list of people who receive salary or wage payments from a business. The payroll records will show how much your employees have earned during each pay period. They will also show deductions that may have been made from those earnings for taxes and benefits. There are many computer software packages that can help you maintain these records. There are also many payroll service companies that you can contract with to handle payroll processing for you.

You will need to complete a payroll register for every pay period. The register will include the following information for each employee:

- Employee name
- Number of hours worked
- Regular and overtime earnings
- Federal, state, and local taxes deducted
- Social security and Medicare contributions deducted
- Deductions for benefits, such as health insurance, life insurance, and retirement savings plans





© PhotoDisc/Getty Images

Why is it important for a business to carefully estimate its income taxes?

After you create the payroll register, you will prepare payroll checks. Most businesses use voucher checks for their payrolls. Voucher checks have a statement of earnings and deductions attached to them. The statement shows employees how their pay was calculated.

Tax Records

You will have to make several different kinds of tax payments as a business owner. These include income taxes, payroll taxes, and sales taxes.

INCOME TAX Businesses that earn profits must pay income tax. These taxes are paid quarterly, or every three months. Income tax must be prepaid at the beginning of a quarter, so you will need to estimate your income taxes. If you fail to make these payments or you underestimate how much tax is due, you may have to pay a penalty. You could also be subject to criminal penalties for tax fraud.

PAYROLL TAXES AND DEDUCTIONS By law, you are required to

deduct taxes from your employees' paychecks and submit these taxes to the government. As an employer, you are also required to pay unemployment insurance taxes and a portion of Social Security taxes based on the earnings of your employees. Your employees may ask you to take voluntary deductions from their earnings to cover health or dental insurance. If you deduct this money from employees' earnings, you are required to send it to the companies that are providing the insurance coverage.

BE YOUR OWN BOSS

You own a home remodeling business in your community. You have one full-time employee working for you. Research the types of federal, state, and local taxes you will need to withhold from your employee's paycheck. Create a table listing the types of taxes to withhold. For each one, describe how you would determine the amount of taxes to withhold.



SALES TAX Retail businesses are required to charge sales taxes on goods or services. If you own a business that collects sales tax, every month you will have to deposit the tax you collect into a special bank account that belongs to the government. Sales taxes are based on a percentage of sales. The actual percentage charged varies from state to state and can vary within a state if the local county or city also assesses a sales tax.

Checkpoint

What kinds of bank, payroll, and tax records do you have to keep?

9.3 Assessment

THINK ABOUT IT

1. Eliza Conner owns a small clothing boutique. Eliza uses her personal checking account for both business and personal needs. How would you convince Eliza that she should open a separate bank account for her business?
2. Why is it important to keep accurate and up-to-date bank, payroll, and tax records?

MAKE ACADEMIC CONNECTIONS



3. **MATH** As a business owner, you should reconcile your bank statement each month when you receive it. Using the Activity CD, open the activity "Bank Reconciliation." Print a copy and complete the activity.
4. **MATH** Scott Belville, owner of Flowers on Main, completed an aging table for his accounts receivable. The column totals are shown below. Complete the percent of total row for Scott.

Customer	Amount	0–30 Days	31–60 Days	Over 60 Days
Totals	\$6,500	\$2,300	\$3,100	\$1,100
Percent of total	___?___	___?___	___?___	___?___

5. **COMMUNICATION** Assume you are Kim Smith, the owner of Photo Memories. Look at the aging table on page 255. You have decided that no more orders will be filled for Mark Stern until his account balance is paid in full. Write a letter to Mr. Stern to inform him of your decision. Provide payment options to help Mr. Stern pay off his account balance.



TEAMWORK

Working with team members, discuss the pros and cons of maintaining electronic records versus manual records for your business. What are some ways to resolve the cons of maintaining electronic records? Which way do you think is best? Why?



Sharpen Your Entrepreneurial Skills

Prepare a Resume

Along with your personal financial statement, a resume should be part of your business plan's appendix of supporting documents. Potential lenders and investors will want to know about you, the entrepreneur. Knowing about your skills, experience, and character will help them decide whether or not investing in your business is a good idea. A personal resume describes your skills and experience to help prove you have the ability to own and manage a business. Your resume should demonstrate that your background is suitable for the business you wish to start and should convey to readers your career goal, self-image, communication skills, ability to achieve results, and personal character.

A well-written resume includes the following information:

1. Name, address, telephone number, and e-mail address.
2. A statement describing your career objective and why you are qualified to reach the objective.
3. A list of your work experience arranged by date with the most recent work experience listed first. Include a brief description of responsibilities and accomplishments for each position.
4. A description of your education and any other training programs in which you have participated.
5. A list of personal activities that demonstrate that you are reliable and ambitious. Include community service activities, any hobbies you have that relate to your business, and any awards or honors you have received.
6. The names and contact information of three references who can verify the information on your resume.

When preparing your resume, try to keep it to one page in length. Be sure that it is well organized and includes only significant information that gives evidence of your abilities. Proofread your resume carefully to ensure that your spelling and grammar are 100 percent correct.

TRY IT OUT

Using the Activity CD, open the activity "Prepare a Resume." Print a copy of the sample resume and review it. Then complete the questionnaire to help you compile your own resume for the business idea you have been working on in the *Build Your Business Plan Project*. Your resume should communicate your ability to start, run, and manage the business. Include your resume in the appendix of your business plan.



© Digital Vision/Getty Images

Chapter 9 | Assessment

SUMMARY

9.1 Finance Your Business

1. As an entrepreneur, you must prepare a list of startup costs to determine how much money you will need to start your business. You should also prepare a personal financial statement based on the formula: $\text{Total assets} - \text{Total liabilities} = \text{Net worth}$.
2. Equity capital is money invested in a business in return for a share in the profits of the business. Sources of equity capital include personal contributions, friends and relatives, and venture capitalists.
3. Debt capital is money loaned to a business with the understanding that the money will be repaid. Sources of debt capital include friends and relatives, commercial banks, and government agencies such as the SBA.

9.2 Pro Forma Financial Statements

4. The cash flow statement describes the way that cash flows in and out of your business and uses the following basic formula: $\text{Cash receipts} - \text{Cash disbursements} = \text{Net cash flow}$.
5. The income statement shows the business's revenues and expenses incurred over a period of time and the resulting profit or loss. It can help you forecast how well your business can expect to perform in the future.
6. The balance sheet is a financial statement that lists what a business owns, what it owes, and how much it is worth, using the accounting equation: $\text{Assets} = \text{Liabilities} + \text{Owner's Equity}$.

9.3 Recordkeeping for Businesses

7. Businesses initially record transactions in journals. The transactions are then posted to accounts in the general ledger. More detailed records of certain general ledger accounts, such as accounts receivable, are kept in a subsidiary ledger.
8. You will need to keep accurate and up-to-date bank, payroll, and tax records. You must keep your bank records balanced and prepare a bank reconciliation each month. If you have employees, you will need to prepare a payroll register for every pay period. You will also have to track and pay income, payroll, and sales taxes at regular intervals.

What do you know now?

Read Ideas in Action on page 237 again. Then answer the questions a second time. How have your responses changed?

VOCABULARY BUILDER

Match each statement with the term that best defines it. Some terms may not be used.

1. The difference in what you own and what you owe
2. A financial statement that shows a business's revenues and expenses incurred over a period of time
3. Money invested in a business in return for a share in the profits of the business
4. A list of people who receive salary or wage payments from a business
5. A financial statement that describes the way that cash flows into and out of your business
6. Any business activity that changes assets, liabilities, or net worth
7. Property that the borrower forfeits if he or she defaults on a loan
8. Accounting records of the business transactions you make
9. Money loaned to a business with the understanding that the money will be repaid
10. The relation between the dollars you have borrowed and the dollars you have invested in your business
11. Individuals or companies that make a living investing in startup companies
12. A financial statement that lists what a business owns, what it owes, and how much it is worth at a particular point in time

- a. account
- b. balance sheet
- c. cash flow statement
- d. check register
- e. collateral
- f. debt capital
- g. debt-to-equity ratio
- h. equity capital
- i. income statement
- j. journals
- k. net worth
- l. payroll
- m. transaction
- n. venture capitalists

REVIEW YOUR KNOWLEDGE

13. Which of the following would be a startup cost?
 - a. computer for the business
 - b. monthly utility bill
 - c. monthly rent expense
 - d. weekly payroll
14. Loans that are guaranteed with property are called ____?__.
15. You have decided to try to finance your business with equity financing. Who should you approach to invest in your business?
 - a. local bank
 - b. Small Business Administration
 - c. friends and family
 - d. Department of Housing and Urban Development
16. Which of the following would most likely be accepted as collateral for a secured loan for \$25,000?
 - a. \$32,000 automobile that is paid in full
 - b. \$12,000 of home equity
 - c. \$2,500 computer system
 - d. apartment that you rent
17. Which of the following is *not* a reason that a bank may reject your loan application?
 - a. business is a startup
 - b. owner invested \$30,000
 - c. business plan is sloppy
 - d. owner has no experience

18. **True or False?** The Small Business Administration offers loans to businesses in the same way that a commercial bank does.
19. Which of the following would *not* be included on a cash flow statement?
 - a. Sale to customer on account
 - b. Payment received from a customer on account
 - c. Payment made to a vendor for new equipment
 - d. Funds of \$4,000 received from bank loan
20. You are using five separate journals to record your business transactions. In which journal would you record a sale of merchandise if the customer pays you cash at the time of the sale?
 - a. sales journal
 - b. cash payments journal
 - c. cash receipts journal
 - d. purchases journal
21. **True or False?** Taxes that you withhold from employees' paychecks are deposited into your bank account until the employee files an income tax return.
22. **True or False?** If your cash receipts are less than your cash disbursements, your business has a negative cash flow.
23. A potential investor or bank would want to see all of the following financial documents *except*
 - a. cash flow statement
 - b. startup costs
 - c. personal financial statement
 - d. journal

APPLY WHAT YOU LEARNED

24. You plan to open a retail sportswear store. You will hire several employees to help run the store. What types of journals do you need to keep for such a business? Why? What kinds of bank, payroll, and tax records will you have to maintain? How could you use a computer to help you keep and manage your records?
25. You plan on opening Rashida's Beauty Salon. You have listed your projected monthly revenues, expenses, and taxes below. Prepare a pro forma income statement based on this information.

Revenues	\$15,000	Insurance	\$ 750
Cost of goods	2,550	Rent	1,000
Supplies	1,100	Utilities	650
Salaries	4,800	Taxes	1050

MAKE ACADEMIC CONNECTIONS

26. **MATH** You own a store that sells video games. You owe \$25,000 to video game vendors; you have a ten-year bank loan of \$50,000; your bank account balance is \$13,000; you own inventory worth \$57,000; you have \$2,000 in account receivables; and fixed assets are \$22,000. What are your total assets, liabilities, and owner's equity?
27. **COMMUNICATION** Conduct a phone interview with the manager of a local bank to find out what kinds of loans they offer to small businesses. Specifically, ask them about their secured loans, unsecured loans, and SBA-backed loans. Write a one-page report on your findings.

WHAT WOULD YOU DO?



You are working on your resume for your business plan. After listing your experience, you think it might appear as if you do not have the adequate experience and skills to successfully start and run your business. You consider enhancing your resume by adding some additional job experiences that you haven't had in order to make it look better for potential investors and lenders. Do you think it will matter? Do you think anyone will ever actually check your experiences or references? What might be the result if they do check? What would you do?

BUILD YOUR Business Plan *Project*

This activity will help you continue with the development of a business plan for your business idea.

1. Estimate your startup costs for your business and prepare a personal financial statement to determine your net worth.
2. Determine how much money you need to begin your business. Decide if you will obtain equity and/or debt financing. Will you use personal contributions or borrow from friends and relatives, venture capitalists, a commercial bank, the SBA or other government agency, or a combination of these resources? Write why you think one or more of these financing methods will work for your business.
3. Determine your projected cash receipts and cash disbursements for the first year of your business. Prepare a pro forma cash flow statement. After doing so, prepare pro forma cash flow statements based on worst-case and best-case scenarios.
4. Determine your projected revenue and operating expenses for the first year of your business. Estimate the amount of income taxes you will have to pay. Prepare a pro forma income statement.
5. Make a list of your assets and liabilities. Prepare a pro forma balance sheet.
6. Determine what types of journals you will keep for your business. For each type, give an example of a transaction that will be recorded in that journal. What accounts will your business have?
7. Contact two local banks and obtain information about commercial checking accounts. What are the rates? What types of special services or products are offered to small business owners?
8. Create a payroll register for your business. Contact your state and/or local government to find out what taxes must be deducted from employees' pay. Find out how the taxes are calculated. Are there any other deductions that will be made? If your business collects sales tax, find out what the rate is in your state or county.

Planning a Career in Finance



"My brother Boyd, an accountant, got tired of the demanding hours required while working at a large accounting firm. Tax season was particularly demanding on his family. His wife is an attorney with her own strenuous workload. They decided he should stay home with the kids and start a part-time business as an accountant for small businesses."

How do small businesses manage their finances to comply with legal requirements? How can a small business understand how changes in financial reporting laws affect them?

Accountants help individuals and corporations prudently manage their finances. Asset management, design of accounting information management systems, and tax preparation are some of the services provided by accountants.

EMPLOYMENT OUTLOOK

- Faster than average job growth is anticipated.
- Changes in accounting-related legislation will fuel demand for accountants to help corporations meet regulatory requirements.
- Accountants will be needed to help prevent and circumvent financial fraud.

JOB TITLES

- Accounting Manager
- Controller
- Financial Auditor
- Certified Public Accountant (CPA)
- Cost Accountant
- Financial Reporting Accountant

NEEDED SKILLS

- A Bachelor's Degree with a major in accounting, finance, or business administration is required.
- Advancement may require a Master's Degree in accounting or an MBA.
- Professional certifications in various accounting specialties for certain positions.
- Continuing education is required in most states.

What's it like to work in Finance

Boyd, an independent Certified Public Accountant, had a variety of clients. Today, he was in a monthly meeting with the owner of a home décor boutique store. Evaluating the financial components of the business, including inventory levels, expenditures, payroll, accounts receivable, and taxes was a critical part of the meeting.

Boyd also helped his client assess the value of various promotions the store ran periodically throughout the year. Analyzing the success of promotions by comparing promotional costs to incremental revenue increases helped the boutique owner understand which promotions were profitable.

At the conclusion of the meeting, the client asked Boyd to look into whether it would be financially wise to buy a building to house the boutique or whether the store should remain in its current rented location.

What about you? Would you like to help businesses improve their financial performance by helping them manage the financial side of their business?



BUSINESS FINANCIAL PLAN

A financial plan is essential to the success of any business enterprise. You and your teammates are challenged to establish and develop a complete financial plan for a successful business that wants to expand into two surrounding communities. The financial plan must be economically and financially sound within a realistic time frame.

You will prepare a synopsis of 500 words or less that summarizes the loan needed to expand a successful local business into two surrounding communities. Plans must not exceed 15 pages and will include the following content: Synopsis; Company Description (legal form of business, company mission, company governance, company locations, long- and short-term goals); Operations and Management (business facilities, management personnel, workforce); Target Market (current target market and future sales potential); Financial Institution (name of financial institution and rationale for choosing the financial institution); Loan Request (purpose, amount, planned expenditures, planned repayment for the loan and projected future stability of the company); and Supporting Documents.

You will have seven minutes to present your plan, and the judge(s) will have three minutes to ask questions.

PERFORMANCE INDICATORS EVALUATED

- Explain the opportunity for business expansion.
- Present convincing rationale for expanding a business into two surrounding communities.
- Develop a complete financial plan for a business venture.
- Request a business loan from a financial institution.
- Present financial information to obtain a loan from a financial institution.
- Organize a financial proposal for a growing business.
- Manage time and information for an effective presentation.

Go to the FBLA web site for more detailed information.

Think Critically

1. Why does a financial institution want to know the future sales potential of the business's target market?
2. What does a business's workforce have to do with a business loan?
3. Why should the business project how quickly a loan will be repaid?
4. Why must the team describe the target market demographics for the two new proposed locations for the business?

Chapter 10



© PhotoDisc/Getty Images

Operations Management

10.1 Operating Procedures

10.2 Inventory Management

10.3 Financial Management

school.cengage.com/entrepreneur/ideas

IDEAS IN ACTION

Entertaining and Planning

Twin brothers, Erik and Andrew Jensen, wanted some special entertainment for their parent's twenty-fifth wedding anniversary party. They were not able to find anyone to provide what they wanted, so they decided to DJ the party themselves, using a mix of equipment they had both purchased and rented. Soon guests from the party started requesting their services, and Twin Spin DJ and Entertainment was started!



© Andrew Jensen

Andrew Jensen, President & CEO, Jx2 Productions

To accommodate changes in the business over the next year, they changed the name to Jx2 Productions. As the business continued to grow and change from a hobby to a career, the brothers found a need to develop a formal business plan. Eventually, Andrew bought out his brother's share of the business and changed the form of ownership to a limited liability corporation. The business expanded to offer video services, event planning, and bookings for hypnotists, comedians, jugglers, and other live entertainers.

As the services offered expanded, Andrew found a need for a better way of presenting the business on paper and on the Web. So, he hired a professional graphic design company to create a company logo to display in advertisements and on the company web site. The logo presents a consistent, professional look and has been important to the image of Jx2 Productions.

Andrew uses the teamwork approach in running his business. He serves as the team leader and holds monthly and sometimes weekly meetings with his staff of three to keep everyone informed and on the same page. They work together to come up with new marketing ideas. He feels that this is important because his DJ's are also his salespeople. It is very important for them to have the right information to communicate to potential clients when they are out on assignments.

Jx2 Productions has been located in the Student Business Incubator (SBI) at Springfield Technical Community College for the past two years. This location has offered Andrew opportunities to grow the business. In addition to offering space and a convenient location, the SBI offers networking and training sessions on finances, advertising, teamwork, and time management.

Andrew encourages other students to start their own business if they feel it is right for them. His advice is to follow your dreams, your heart, and whatever drives you to get up every day.

What do you know?

1. What is the advantage to Andrew of forming Jx2 Productions as a limited liability corporation?
2. Do you think the image of a company is important?
3. What do you think of Andrew's teamwork approach to running his business?

10.1

Operating Procedures

Goals

- Define the five functions of management.
- Describe four types of policies that should be included in an operations manual.

Terms

- manager
- management
- organizational structure
- authoritative management
- democratic management
- operations manual

Focus on Small Business

From entrepreneur to manager

Avery had been running her alterations business alone for almost six months. The business grew, and Avery hired three employees. With others to help operate the business, Avery decided to take a vacation.

Two days into her vacation, her cell phone began ringing nonstop. The three employees were fighting among themselves about who was supposed to do what. No one wanted to answer the phone, and customers were becoming frustrated trying to find out when their clothing alterations would be completed. Avery had to return home to get her business under control!

Work as a Team Discuss with your teammates the shift that must be made from entrepreneur to manager when the business hires employees. Do you think all entrepreneurs make good managers? What skills do you think good managers should have?



© PhotoDisc/Getty Images

Managers are responsible for business operations.

Management Functions

Once you open your business and have people working for you, you become a manager. A **manager** is the person responsible for planning, organizing, staffing, implementing, and controlling the operations of a business. These are functions that all managers must perform, no matter the size or type of business that they manage.

Management is the process of achieving goals by establishing operating procedures that make effective use of people and other resources. All functions of management work together and are continuous.

Planning

Planning involves analyzing information, setting goals, and making decisions about what needs to be done to move the business forward.

The planning activities must be performed in a timely manner. In business you often hear the saying, “time is money.” If you waste time in the planning process, you can lose money for your business. There are three types of planning that should take place in any organization.

- **Strategic planning** Setting broad, long-range objectives to achieve the long-term goals of your business is called strategic planning. You should think three to five years ahead when doing strategic planning. Envision where you want your business to be at that time and what it will take to get you there.
- **Intermediate-range planning** Preparing detailed plans and strategies for achieving goals within a one-year period is intermediate-range planning. You should include target dates for the completion of the tasks that will lead to the accomplishment of your goals.
- **Short-term planning** Planning for the day-to-day operations of the business to achieve the goals and objectives set in intermediate-range planning is called short-term planning. Rules, policies, procedures, and budgets are important components of short-term planning.

Planning is an ongoing process. Entrepreneurs frequently refer back to their business plan for guidance. Likewise, the planning that you do once your business is up and running will help you maintain focus and keep your business on track. Once plans are in place, it does not mean they must be followed exactly. Plans can be revised as needs change.

Organizing

Organizing is identifying and arranging the work and resources needed to achieve the goals that have been set for your business. Included in the organizing function are the following:

- **Assignment of tasks** You will need to decide which employee will be responsible for which tasks in the business. As you start your business, you will have to determine how many employees you will need and what their duties will be.
- **Grouping of tasks into departments** As your business grows, you will need to organize departments. You will have to decide which tasks are closely related and group them accordingly. Some of the department titles that businesses use include Accounting, Marketing, and Human Resources.
- **Organizational structure** As your company grows, you will need an organizational structure. An **organizational structure** is a plan that shows how the various jobs in a company relate to one another. It is often represented in a chart and indicates the working relationships within the business.
- **Allocation of resources across the organization** There will never be enough resources for all the needs and wants of everyone in your business. There must be a plan for distributing the available resources for their most efficient use across the company. This is done by creating budgets based on requests from the departments within the company.

★ Develop Your Reading Skills

Before you begin reading, skim the chapter and note the headings and boldface words. Think about what you will be learning as you read the chapter.



Staffing

Staffing includes all of the activities involved in obtaining, training, and compensating the employees of a business. Because a company is only as good as the people who work for it, the staffing function is critical to the success of a business.

Implementing

Implementing involves directing and leading people to accomplish the goals of the organization. Implementing is accomplished through communicating directions, assignments, and instructions to your employees. In order to effectively implement the work of the organization, managers must develop a management style that will motivate employees to perform at a high level. *Management style* is the way a manager behaves toward and works with employees. Managers use different styles based on the characteristics of the employees being managed, the type of work assignment, and the importance of the work being performed. An experienced and effective manager can change the style as needed.

AUTHORITATIVE MANAGEMENT A management style in which the manager is directive and controlling is called **authoritative management**. This style is also called *directing* or *autocratic management*. The manager makes the major decisions and closely monitors the work of the employees to be sure the work is done correctly. This management style is often used in a crisis situation when there is not enough time to let the group participate in the decision-making process. It is also appropriate when working with a new group of employees who do not have previous experience in the type of work being performed.

NETBookmark

There are many other categories of management styles besides the traditional ones described in your textbook. Corporate performance expert Dr. Ichak Adizes has identified four different managerial styles: producer, administrator, entrepreneur, and integrator. Access school.cengage.com/entrepreneur/ideas and click on the link for Chapter 10. Take the test on the Management Vitality web site to determine your personal style. Do the results seem accurate? Why or why not? Which of Adizes' styles would fall under the category of authoritative management? Democratic management? Do any of Adizes' styles seem to incorporate elements of mixed management?

school.cengage.com/entrepreneur/ideas

DEMOCRATIC MANAGEMENT A management style in which employees are involved in decision making and the manager provides less direction is called **democratic management**. This style is also called *participatory management*. A manager of a group of experienced employees who work well together does not have to be directive and controlling. Employees like to be involved in the planning and decision making that affects their work.

MIXED MANAGEMENT Combining authoritative and democratic management styles is called mixed management. Different employees prefer different management styles. Some employees prefer to be told what to do and want someone else to do the day-to-day decision making. Others feel that if they are not involved in the decision-making process, the manager does not trust

them. An effective manager should be prepared to use mixed management in order to meet the needs of the business and its employees.

Controlling

Controlling is the process of setting standards for the operation of a business and ensuring those standards are met. Some of the ways that you can determine if standards are being met are as follows:

- Compare actual revenues and expenses with what was projected
- Observe business operations and determine if they are running effectively
- Inspect products and services to ensure they are meeting performance standards

If standards are not being met, it will be necessary for managers to make changes. Changes may include hiring new employees, upgrading to higher-quality production materials, or increasing the budget for a specific area. You may also decide to change operating procedures such as work processes and work flow. As part of the control function, you will routinely review your plans and make adjustments.

Checkpoint

What are the functions of management?

Operations Manual

As your business grows, you will find that a detailed operations manual is an essential tool for operating your business effectively and efficiently. An **operations manual** contains all of the rules, policies, and procedures that a business should follow in order to function effectively. You can also have a separate *company* or *employee handbook* that details the rules, policies, and procedures that apply to employees. Just as you spent time developing your business plan, it is important to spend time detailing the operations of your business.

Your operations manual should include the rules, policies, and procedures that guide your business practices. *Rules* outline the appropriate behavior and actions of those that work for you. All employees should be treated the same way when it comes to rules. *Policies* serve as a guideline for daily operations. They are established to make the business run efficiently and may apply to both employees and customers. *Procedures* are a series of steps and actions that employees must follow to complete an activity. They are instructions on how to perform a job task correctly. Procedures are more specific than rules.



Why does a business need a company handbook?

© PhotoDisc/Getty Images

© PhotoDisc/Getty Images



Why is it important for a business to establish customer service policies?

Rules, policies, and procedures are established to make the business run efficiently. As a business owner, it is important for you to remember that sometimes you have to make exceptions to rules, policies, and procedures because not all situations are the same.

Operating Policies

Policies related to hours of operation should be established. You should set daily operating hours that are convenient for your customers. For many years, banks were open Monday through Friday from 9 a.m. to 4 p.m. when most people were working. In order to

meet the needs of their working customers, many banks have extended hours to 6 p.m. or 7 p.m. and are open on Saturdays.

Customer Service Policies

Customer satisfaction is one of the main goals of any business. It is important to have a policy for customers who need to return a product or have a follow-up service. Products do not always meet the expectations of customers, and a service might not be performed to the customer's satisfaction the first time. A policy for replacements, refunds, or repairs will help maintain goodwill. Other customer service policies can include payment options regarding cash, check, and credit cards.

Rich's Department Store, a long-time Atlanta business, operated under the philosophy that all people are inherently honest and that going the extra mile for customers would benefit the company in the long run. Rich's was known to provide refunds on merchandise not carried by its stores and to provide full refunds on noticeably used items—no questions asked.

Delivery Policies

Some businesses provide delivery services along with the sale of their products. Delivery may be required because of product size or out of convenience for the customer. A customer might be more likely to purchase a large appliance from a company that offers delivery, since most people cannot put a refrigerator or washing machine in their vehicles. Many restaurants offer delivery service for food as a convenience to their customers. You will need to determine whether you will offer delivery services for the products you sell, whether you will charge a delivery fee, and whether you will guarantee delivery within a certain timeframe.

Safety Policies

It is important that you have policies in place that provide for a safe environment for your customers and employees. Instruction in safety procedures should be part of employee training. Employees should know how to operate equipment safely and be required to wear the necessary protection gear. Employees should also be briefed on emergency plans for fires, tornadoes, and other disasters. Signs should be placed in strategic locations reminding employees of safety procedures in the workplace. You should also provide warnings to customers so that they do not enter employee-only areas. Caution cones can be placed where unsafe conditions exist.

Checkpoint

What type of information should be included in an operations manual?

10.1 Assessment

THINK ABOUT IT

1. Why do you think it might be difficult for some entrepreneurs to become managers?
2. Why do you think it is important to develop an operations manual for a business?

MAKE ACADEMIC CONNECTIONS

3. **PROBLEM SOLVING** You have been named manager of the children's department of a retail clothing store. Sales are down in the department. You have five employees in your department. Two have been working in the department for three years. The other three are new to the store and have no retail experience. Describe the management style you will use to lead the department and increase sales.
4. **COMMUNICATION** Good customer service policies are essential to the success of a business. Think about the customer service provided by businesses in your area. Choose a business and write a paragraph describing what is good about the customer service provided and another paragraph with suggestions for improving customer service.



TEAMWORK

Working in a small group, describe the traits of the perfect manager. Explain why each trait is important.



10.2

Inventory Management

Goals

- Prepare a purchasing plan for inventory.
- Describe the perpetual and periodic inventory methods.
- Determine how much inventory to keep in stock.

Terms

- perpetual inventory method
- stock card
- point-of-sale (POS) software system
- periodic inventory method
- stock turnover rate

Focus on Small Business

How much to buy?

Matthew was starting his own frame store, Matt's Frames. He had previously worked part time in a framing store and had learned a great deal about the business. Matthew considered how much inventory he would need initially. He knew from his previous experience that the first few months of the year would be slow but that business would pick up as Mother's Day and graduations approached. Because people purchase frames as wedding gifts, Matthew knew his business would pick up in the summer during the height of the wedding season. Another sales peak would occur during the holiday season.

Because he was opening his store in February, Matthew decided he would start out with a small inventory of basic framing supplies and focus on specialty frames for Valentine's Day. Then he would increase his inventory for the spring and summer seasons.

Work as a Team Do you think that Matthew is doing the right thing by starting out with only basic framing supplies? Why do you think he intends to increase his supplies as spring and summer approach?



© PhotoDisc/Getty Images

Business owners must carefully plan to meet inventory needs.

Meet Inventory Needs

Inventory is the stock of goods a business has for sale. Successful inventory management involves balancing the costs of inventory with the benefits of having inventory in stock. Maintaining inventory is costly to a business, and it must be well managed if you are going to make a profit. Direct costs of inventory include storage, insurance, and taxes, in addition to the purchase price of the inventory. Some of the concerns about inventory that managers must address include the following:

- Maintaining a wide assortment of stock, but keeping adequate quantities of fast-moving items
- Increasing inventory turnover, but maintaining a high level of service
- Keeping stock levels as low as possible without sacrificing service or performance as a result of stockouts
- Obtaining lower prices by making bulk purchases, but not ending up with slow-moving inventory
- Having adequate inventory on hand, but not ending up with out-of-date items



© PhotoDisc/Getty Images

How can a store meet both its inventory needs and its customers' needs?

Purchasing Plan

The most important aspect of inventory management is having items in stock when they are needed. This involves planning ahead to determine inventory needs, placing purchase orders for the items in advance, and scheduling deliveries to arrive at the point in time when you need the items. Inventory management also involves determining when you need the most inventory in stock, when reorders should be placed, and when you should discontinue stocking an item.

The amount of inventory you need to purchase can be calculated from the sales forecast. You must look at how many units you need to add to the inventory you already have in stock to reach your sales objective. The formula for calculating inventory needs is:

$$\text{Beginning inventory} + \text{Purchases} - \text{Sales} = \text{Ending inventory}$$

Alan has a beginning inventory worth \$40,000 in his automobile parts store and expects to sell \$80,000 over a period of six months. He wants to have \$25,000 of inventory at the end of the six-month period. Alan uses the formula to calculate his purchases.

Beginning inventory	+	Purchases	-	Sales	=	Ending inventory
\$40,000	+	?	-	\$80,000	=	\$25,000
		?	-	\$40,000	=	\$25,000
		?			=	\$25,000 + \$40,000
		?			=	\$65,000

Alan must purchase \$65,000 in inventory during the six-month period. He now needs to plan for the purchase and delivery of the inventory. He does not want to purchase the entire inventory and have it delivered at the same time because he does not have the cash to pay for it all at once, nor does he have the storage space. Alan decides to make his major purchases in the spring when people are beginning to get their cars ready for vacations and summer



travel. He knows from past experience that he will sell more from March through June and that January and February are slower months. Based on this information, Alan prepares a detailed purchase plan to show how much inventory he will purchase each month during the six-month period.

PURCHASE PLAN FOR AUTOMOBILE PARTS							
	January	February	March	April	May	June	Total
Beginning inventory	\$40,000	\$33,500	\$29,500	\$25,300	\$25,600	\$25,050	
+ Purchases	4,500	4,500	10,800	16,800	14,200	14,200	\$65,000
– Sales	(11,000)	(8,500)	(15,000)	(16,500)	(14,750)	(14,250)	\$80,000
= Ending inventory	<u>\$33,500</u>	<u>\$29,500</u>	<u>\$25,300</u>	<u>\$25,600</u>	<u>\$25,050</u>	<u>\$25,000</u>	

Checkpoint

What are some of the concerns managers have regarding inventory?

Track Your Inventory

Most businesses have to keep the products they sell in stock as a convenience to their customers. To avoid running out of items your customers want, you will need to keep track of your inventory levels. You will also need to determine how much you can afford to keep in stock at any given time.

Tracking your inventory can be done in two different ways. You can use the perpetual inventory method or the periodic inventory method. Regardless of the inventory method you use, you will need to take a physical inventory at least once or twice a year.

BE YOUR OWN BOSS

You own a small hardware store located on the Gulf Coast. Weather forecasters are predicting higher-than-average hurricane activity in your region for the upcoming season. You know that if a hurricane comes to your area, there will be a high demand for plywood, generators, batteries, and other hurricane preparedness supplies. You have limited storage space and limited funds to invest in inventory, but you realize the chance to increase sales and profits. Outline a plan for managing your inventory needs. Explain your decisions.

Perpetual Inventory Method

The **perpetual inventory method** keeps track of inventory levels on a daily basis. This method can make your business more efficient. It can also ensure that you never run out of stock. This method uses stock cards or a computer to keep track of the inventory you have. A **stock card** is a paper inventory record for a single item. Regardless of whether you use stock cards or maintain electronic inventory records, you should record the following items:

- A description of the item
- A stock number for identification purposes
- Any receipt of inventory, the number of units received, and the date of the transaction
- Any sale of inventory, the number of units sold, and the date of the transaction
- The amount of inventory you currently have
- The minimum amount you want to keep in inventory, often referred to as the *reorder point* because it indicates when you should place an order to receive more units
- The maximum amount you want in inventory at any time

Lei Woo owns a toy store. Lei uses her computer to track inventory levels on a daily basis. She creates a low stock report, which shows the items she needs to reorder. It also shows how many units of each item Lei needs to order so that she can restock to the maximum level.

LOW STOCK REPORT				
ITEM	STOCK NUMBER	MAXIMUM	REORDER POINT	NEED TO ORDER
Building blocks	Q323	15	7	8
Doll houses	K393	4	2	2
Playing cards	S222	25	12	13
Stickers	S494	50	20	30

USE A COMPUTER Businesses that sell hundreds of items usually track inventory electronically. Inventory software programs let you track usage, monitor changes in unit dollar costs, calculate when you need to reorder, and analyze inventory levels on an item-by-item basis.

Many retail businesses use cash registers with a **point-of-sale (POS) software system** that updates inventory records as each sale happens. Bar-code scanners and credit card authorization systems can be integrated into the POS system. With the POS system, you will always have an up-to-date inventory balance. You will also get detailed information on sales that will assist you in the decision-making process for inventory management. You can analyze the sales data, determine how well each item you have in stock is selling, and adjust your purchasing accordingly.

Periodic Inventory Method

Some businesses use the **periodic inventory method**, which involves taking a physical count of your merchandise at regular intervals, such as weekly or monthly. This method will tell you how many units of each item remain in stock. You can then compare your inventory counts to your established reorder points to determine which items need to be restocked. This method is commonly used by small businesses with limited inventory.

Take a Physical Inventory

Even with the perpetual inventory method, you will need to take a physical inventory at least once or twice a year. Your actual inventory may differ from that listed in your perpetual inventory system. The





© Digital Vision/Getty Images

Why should businesses take a physical inventory periodically?

difference can be caused by many things, such as theft, damage to merchandise, or failure to record sales. Taking a physical inventory means counting the number of items you have in stock. You will need to record the date on which you are taking the inventory, the stock number of each item, a description of each item, and the actual number of units in stock.

At least two people should be involved in taking a physical inventory. One person should count the items on hand while the other records the information found. This information can later be entered into a spreadsheet for easy use.

Checkpoint

How does the perpetual inventory method differ from the periodic inventory method?

Manage Your Inventory

The level of inventory you keep in stock depends on three factors:

- The costs of carrying inventory
- The costs of lost sales due to stockouts
- Your stock turnover rate

Costs of Carrying Inventory

Holding inventory can be very costly. These costs are known as *carrying costs*. A business with inventory will always have carrying costs. Carrying costs can become too high if you have too much inventory. Costs can increase for many reasons.

- **Obsolescence** Inventory can be held too long and become old and outdated. People do not want to buy a computer made two years ago. You may be stuck with merchandise you cannot sell.
- **Deterioration** Inventory can deteriorate, forcing you to throw it away or sell it at a discount. If you own a garden store, some plants will need to be sold within a few weeks because they will begin to die.
- **Interest fees** Vendors charge interest on money due to them. If you cannot pay your vendors until you sell your inventory, you will incur an extra expense.
- **Insurance** You will need to carry insurance against theft, fire, and other disasters. Insurance premiums increase as the value of the inventory insured increases.
- **Storage** Inventory takes up space—space that you may be leasing on a square-footage basis. If you run out of room, you will need to lease additional space.

Costs of Being Out of Stock

Being out of stock can cost you money. If you are out of the items your customers want, you will lose sales. If customers repeatedly fail to find what they are seeking at your business, you could also lose customer loyalty. You must weigh the costs of being out of stock against the costs of carrying more inventory.

Stock Turnover Rate

A supermarket might sell hundreds of cans of soft drinks every day but only 12 jars of marmalade. The **stock turnover rate** is the rate at which the inventory of a product is sold and replaced with new inventory. It shows how many times a year you sell all of your merchandise. A store that purchases inventory four times a year and sells all of its inventory in that same year has a stock turnover rate of 4.

Famous Entrepreneur

Ganz Family

What do a stuffed animal toy and the Internet have in common? Plenty, if you are in the Ganz family business. They have taken the stuffed animals children play with and made them a portal to the Internet and the Webkinz World.

Shortly after World War II, Samuel Ganz came to the United States from Romania and settled in New York. At about the same time, his sons Sam and Jack settled in Toronto, Canada. In 1950, Samuel went to visit his sons and took along a prototype for a doll. Sam and Jack asked some local toy stores if they would be willing to sell the dolls. After making a few contacts and holding family discussions, Ganz Toys began business!

In the 1980s, Ganz Toys began to focus on gift retailers and added a line of plush gift toys. Under the direction of Howard Ganz, Samuel's grandson, the privately held family company became the top toy company in Canada. Today, the company is known simply as Ganz.

In 2005, Ganz introduced the Webkinz, which quickly became a big hit. The lovable plush pets come with a unique secret code on the label. The code allows entrance into



Why do you think Webkinz are so successful?

the Webkinz World on the Internet. There, an electronic version of the pet can be adopted for virtual interaction. More than two million units have been sold and one million users have registered on the Webkinz web site. The Ganz family business is committed to a future filled with excitement and innovation.

Think Critically

What inventory challenges do you think the success of Webkinz brought to Ganz?

Stock turnover rates vary from industry to industry. You should contact the trade association for your industry or talk to other entrepreneurs in your field to find out the turnover rate for the items you carry.

Turnover rates can help you determine how much inventory to keep in stock. To find out how many months of inventory you should keep in stock, divide 12 (the number of months in a year) by the stock turnover rate.

Brad Wilson owns a retail store. The stock turnover rate in his industry is 6. This means that he needs to keep two months worth of inventory in stock at all times.

$$\begin{array}{ccccccc} \text{Months in year} & \div & \text{Stock turnover rate} & = & \text{Months of inventory to stock} \\ 12 & \div & 6 & = & 2 \end{array}$$

Checkpoint

What three factors determine the amount of inventory you keep in stock?

10.2 Assessment

THINK ABOUT IT

1. Why do you think a purchasing plan is essential to good inventory management?
2. What do you think are the benefits of using the periodic inventory method? The perpetual method?
3. Do you think you could still manage your inventory well if you did not know the turnover rate for a product? Why or why not?

MAKE ACADEMIC CONNECTIONS

4. **COMMUNICATION** Using the perpetual inventory method, create an inventory tracking report on the computer for at least five inventory items a grocery store would carry.
5. **MATH** Using the Activity CD, open the activity "Inventory Management." Print a copy and complete the activity to help evaluate the inventory needs of Elizabeth's Kitchen Warehouse.



TEAMWORK

Working with teammates, make a list of items that you would sell in a hobby store that caters to teenagers. This is a new business with no inventory on hand. Decide how many of each item you think you could sell in a six-month period. Based on this information, make a purchasing plan for the hobby store showing how much inventory you would purchase each month.

10.3 Financial Management

Goals

- Describe strategies for managing cash flow.
- Evaluate a business's performance through financial statement analysis.

Terms

- cash budget
- gross sales
- net sales

Focus on Small Business

Cash flows in and out

Lars is an independent contractor in the construction business. He has recently completed two big contracts and is eagerly awaiting his next. Lars realizes that demand for his services will be less in the winter months and could also decrease as a result of changes in the economy.

Realizing that there could be months when he does not have money coming in, Lars begins to think about his finances. Although he has cash in the bank today, he knows he has to plan for tomorrow. He needs to manage his cash flow to ensure he can cover his expenses during slower months. Lars understands that he needs to set aside money for a time when he doesn't have any contracts lined up.

Work as a Team Why do you think cash flow is important to a business owner? List the kinds of businesses that you think might have cash flow issues similar to those in Lars' business.



© PhotoDisc/Getty Images

Seasonal businesses must plan their cash flow.

Manage Your Cash Flow

As the owner of your own business, you will need to make sure that you have enough cash to make purchases and pay expenses. To do so, you will have to create a cash budget. You will also have to learn how to manage your cash flow.

Create a Cash Budget

A **cash budget** should show the projections of your cash coming in and going out. To ensure accuracy, it should be based on actual past revenues and operating expenses. A cash budget looks very similar to a cash flow statement, but it has slight differences. Three columns are used to show the estimated cash flow, the actual cash flow, and the difference between the two. This information can help you budget your financial resources. If your cash budget shows you will be short

did you KNOW?

According to the National Federation of Independent Businesses (NFIB), five of the top ten concerns of small-business owners relate to costs. Leading the list is the cost of health insurance, followed by the cost and availability of liability insurance, workers' compensation costs, energy costs (natural gas, gasoline, propane, diesel, and fuel oil), and electricity rates.

of cash in six months, you can begin arranging financing or generating capital now. If your cash budget shows you will have a surplus of cash two years from now, you might use that information in planning how to expand your business.

Many companies use spreadsheets to prepare their cash budgets. The spreadsheet will automatically perform calculations on the amounts you provide. This allows you to instantly see the outcomes of changes in your cash flow.

Mark Matson owns a snow removal business that he runs from his home. He uses a spreadsheet to create a budget for the first three months of the coming year, which is shown below. In his first month, Mark's receipts were higher than he anticipated, but so were his expenses. Even so, Mark came out ahead in his overall net cash amount.

CASH BUDGET MARK'S SNOW REMOVAL SERVICE Month One, 20—

	A	B	C	D
		Estimated	Actual	Difference
1	Cash receipts			
2	Cash sales	\$2,000	\$4,000	\$2,000
3	Accounts receivable payments	\$11,150	\$13,150	\$2,000
4	Tax refund	\$850	\$850	\$0
5	Total cash receipts	\$14,000	\$18,000	\$4,000
6	Cash disbursements			
7	Salaries	\$4,500	\$5,500	-\$1,000
8	Gasoline	\$2,500	\$3,125	-\$625
9	Vehicle maintenance	\$350	\$400	-\$50
10	Utilities	\$50	\$50	\$0
11	Advertising	\$150	\$300	-\$150
12	Insurance	\$500	\$500	\$0
13	Other	\$250	\$250	\$0
14	Total cash disbursements	\$8,300	\$10,125	-\$1,825
15	Net cash increase/decrease	\$5,700	\$7,875	\$2,175

Improve Your Cash Flow

Two businesses with the same level of sales and expenses may have very different cash flows. One business may have a positive cash flow while the other may have a negative cash flow and be unable to cover its expenses. The difference may reflect a different pattern of cash receipts and disbursements.

If your cash receipts will not cover required cash disbursements, you will need to take action to improve your cash flow. You can increase cash receipts, decrease cash disbursements, or perform both actions.

INCREASE CASH RECEIPTS One way to improve your cash receipts is to decrease your accounts receivable by getting customers who owe you money to pay more quickly. To encourage faster payment, you can do the following:

- Offer discounts on bills paid right away.
- Establish tighter credit policies (decrease the amount of time your customers have to pay their bills from 60 days to 30 days).
- Establish a follow-up system for collecting unpaid accounts receivable. Consider hiring a collection agency to track down customers who are considerably late with their payments.
- Hold shipments to customers with large unpaid bills or insist that such orders be paid in advance.

Businesses can have cash flow problems if they start off with too little capital. If your cash flow is inadequate, you may want to increase cash receipts by obtaining more capital. This means securing a loan, investing more of your own money in the business, or finding investors who will provide you with capital in return for a share of your future profits.

WHAT WENT WRONG



Too Big, Too Fast

Webvan was founded in the late 1990s by Louis Borders. Webvan was an online grocery ordering and delivery service. It promised customers delivery in a 30-minute window of time. Initially, customers were excited about this service that was offered in nine U.S. markets: San Francisco Bay Area, San Diego, Los Angeles, Chicago, Seattle, Portland, Atlanta, Sacramento, and Orange County, CA. The company's long-range plans included expansion into 26 cities. The company started with hundreds of millions of dollars from private investors and then raised \$375 million in its initial public offering of stock. At one time, Webvan was worth \$1.2 billion.

But all was not good in the Webvan world. Customers did not sign up as founders hoped they would. But the biggest problem Webvan faced was rapidly disappearing cash reserves. It placed a \$1-billion order with engineering company Bechtel to build high-tech warehouses, bought a fleet of delivery trucks, and purchased state-of-the-art computer systems. The management team of Webvan did not have anyone with any experience in the grocery market, and it tried to get too big, too fast. Even though customers were not happy with long lines and the quality of products in traditional supermarkets, they did not flock to

the online grocery store. In less than two years after its successful initial public offering, Webvan announced it was closing.

Think Critically

1. What are some of the problems Webvan faced during its short-lived operation?
2. Webvan started with a large amount of cash reserves. What caused Webvan to end up with cash flow problems?
3. What changes in operations do you think Webvan could have made that might have helped it be successful?



© PhotoDisc/Getty Images

Too many cash disbursements can lead to business failure.



DECREASE CASH DISBURSEMENTS Another way of improving the cash flow of your business is to reduce your disbursements. This can be done by gaining better control over your inventory and payroll, slowing the rate at which you pay your bills, or reducing your expenses.

Inventory is a large business expense over which you have some control. Reducing this expense will improve your cash flow. You know that carrying inventory is costly. If your business has cash flow problems, check to make sure that you are not holding too much inventory. Reducing your inventory will reduce your accounts payable because you will not be purchasing as much.

Payroll is another large category of expense for businesses. Reducing your payroll can improve your cash flow. Payroll expenses can be decreased by reducing the size of your workforce or reducing the number of hours employees work. It is important to determine your workforce needs before making reductions in this area.

Most of your suppliers will offer credit terms and accept payment at a later date if you pay interest charges. Depending on your cash flow needs, you may want to take advantage of the longest possible credit terms or use a credit card for purchases.

Mark Matson usually pays cash for gasoline and oil for his snow-plow trucks. At the beginning of the winter season in December, his expenses are particularly high and cash receipts low, so he charges his expenses to his credit card. By delaying payment until the following month, Mark improves his cash flow in December. When the credit card bill comes in January, he will have received payment from his customers for the work he did in December and will not have a problem paying the bill.

Other expenses, such as rent, are fixed, so you cannot reduce them. But you can reduce variable expenses, such as advertising, to help improve your cash flow.

Checkpoint

What are some ways you can improve your cash flow?

Prepare and Analyze Financial Statements

To run your own business, you have to be able to understand and analyze financial statements to determine how well your business is performing. Businesses keep many kinds of records and create different kinds of financial statements. Your records and statements can help you analyze your profits as well as set and meet profit goals.

Prepare Financial Statements

When you are starting a business you will prepare pro forma financial statements based on projections. Once your business is up and running, you will prepare financial statements that show actual financial



performance. These financial statements will contain more detailed financial information than the pro forma statements because the business's finances will change as the business grows.

The three most important elements of a company's financial strength are its assets, liabilities, and owner's equity. The value of assets, liabilities, and owner's equity on a specific date are reported on the balance sheet. The balance sheet is usually prepared monthly and at year-end.

The income statement reports revenues, expenses, and the net income or loss over a specific period of time, such as a month, a quarter, or a year. Many businesses will prepare an income statement monthly in order to closely monitor revenues and expenses.

The cash flow statement shows the cash inflows (receipts) and cash outflows (disbursements) for a business during a specific period of time. This statement shows the actual cash a business receives and how that cash is used. Unlike the income statement, which reports revenues not yet received and expenses not yet paid, the cash flow statement reports actual amounts, making it the most valuable financial statement for many business owners.



© PhotoDisc/Getty Images

Would you categorize office equipment as assets, liabilities, or owner's equity? Why?

Analyze Sales

You must know how to use the information in your financial statements to determine the level of sales you need to achieve to earn a profit. Your sales records show sales trends and patterns. You can use these records to forecast future sales and make good business decisions.

ANALYZE SALES BY PRODUCT Analyzing your sales by product can help you make decisions about the kind of inventory to stock. It can help you increase sales and profits.

Emily Lee owns a garden and patio store. Her store has four departments: outdoor furniture, outdoor grills, plants, and garden tools. Emily's sales figures show that almost 57 percent of her annual sales come from the outdoor furniture department, as calculated below.

DEPARTMENTAL SALES • LEE GARDEN AND PATIO

Department	Sales	Percent of total*
Outdoor furniture	\$110,000	56.7
Outdoor grills	37,000	19.0
Plants	24,000	12.4
Garden tools	23,000	11.9
Total	\$194,000	100.0

*Rounded

$$\begin{array}{rcl} \text{Sales of outdoor furniture} & \div & \text{Total sales} = \text{Percent of sales} \\ \$110,000 & \div & \$194,000 = 56.7\% \end{array}$$



The plants department accounts for only a little over 12 percent of sales. Based on these data, Emily decides to reduce the size of the plants department and increase her inventory of outdoor furniture.

Analyze Net Profit on Sales

Your income statement shows whether or not your business is earning a profit. It also tells you how profitable your business is. This information can be very useful in helping you set and meet profit goals. The rate of profit a business earns is often shown as the ratio of its net profit to its sales. This ratio is calculated by dividing net income after taxes by net sales.

$$\text{Net income after taxes} \div \text{Net sales} = \text{Net profit on sales}$$

In order to calculate net profit on sales, a business must first perform math calculations to determine net income after taxes and net sales. All of these calculations are found on the income statement.

CALCULATE NET SALES Jack Hendrick owns a retail store that sells automotive supplies. He wants to find out his net-profit-on-sales. First he must determine his gross sales and net sales. **Gross sales** is the dollar amount of all sales. **Net sales** is the dollar amount of all sales with any returns subtracted. Jack sold \$235,000 worth of merchandise and had \$3,200 worth of merchandise returned. Therefore, his net sales amount is \$231,800.

Gross sales	–	Returns	=	Net sales
\$235,000	–	\$3,200	=	\$231,800

CALCULATE NET INCOME AFTER TAXES Three calculations must be performed to determine your net income after taxes. You must calculate the following:

- Gross profit
- Net income from operations
- Net income before taxes

Gross profit is profit before operating expenses are deducted. Last year, Jack spent \$150,000 for merchandise that he sold. This amount represents his cost of goods sold. Jack subtracts his cost of goods sold from his net sales to find his gross profit.

Net sales	–	Cost of goods sold	=	Gross profit
\$231,800	–	\$150,000	=	\$81,800

Jack's operating expenses include rent, salaries, and similar business expenses. Last year his operating costs were \$39,900. Gross profit minus operating expenses equals net income from operations.

Gross profit	–	Operating expenses	=	Net income from operations
\$81,800	–	\$39,900	=	\$41,900

To calculate net income before taxes, Jack has to subtract one more expense that has not yet been taken into account: interest on loans he has obtained. Last year, Jack paid \$2,400 in interest. He subtracts this



from his net income from operations to get his net income before taxes. If a company has no additional expenses, such as interest expense, the net income from operations equals the net income before taxes.

Net income from operations	–	Interest expense	=	Net income before taxes
\$41,900	–	\$2,400	=	\$39,500

To compute his after-tax income, Jack subtracts the amount he paid in income tax last year, \$12,245, from his net income before taxes. This gives him his net income after taxes for his automotive supply business.

Net income before taxes	–	Income tax paid	=	Net income after taxes
\$39,500	–	\$12,245	=	\$27,255

WHY NET PROFIT ON SALES IS IMPORTANT After all of the above calculations have been performed, the net-profit-on-sales ratio can be calculated. This calculation helps determine how profitable your business is. Jack determines that his profits represent 11.8 percent of his net sales.

Net income after taxes	÷	Net sales	=	Net profit on sales
\$27,255	÷	\$231,800	=	11.8%

Jack can use this figure to assess his profits in two ways. First, he can compare his profit ratio this year with his profit ratio in previous years. If his profit ratio has declined, his business has become less profitable. If the ratio has increased, his business has become more profitable. Jack can also compare his profit ratio with average profit ratios in his industry. If his ratio is lower than the industry average, he may want to figure out what he can do to improve his profitability.

Set and Meet Profit Goals

To run your business effectively, you will need to set profit goals. These goals will reflect the amount of profit you hope to earn from your business during a particular year.

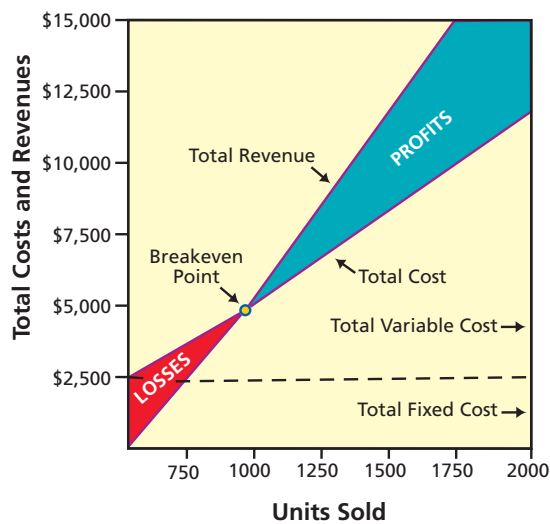
Jack Hendrick would like to increase his profit ratio to 15 percent. He decides to try to increase his sales and reduce his expenses. He begins a frequent-buyer program and offers discounts on bulk purchases. Jack will talk to suppliers with the hope of reducing his cost of goods sold.

Jack would like to increase his profits even more by opening several more stores. He hopes that purchasing his inventory in large quantities will lower his costs significantly.

INCOME STATEMENT Hendrick's Auto Supplies, 20—

Revenue from sales	
Gross sales	\$235,000
Returns	3,200
Net sales	<u>\$231,800</u>
Cost of goods sold	150,000
<i>Gross profit</i>	<u>\$ 81,800</u>
Operating expenses	
Salaries	\$ 26,200
Rent	8,400
Utilities	1,500
Advertising	1,100
Insurance	1,000
Supplies	700
Other	1,000
<i>Total operating expenses</i>	<u>\$ 39,900</u>
Net income from operations	<u>\$ 41,900</u>
Interest expense	2,400
Net income before taxes	<u>\$ 39,500</u>
Taxes	12,245
Net income/loss after taxes	<u><u>\$ 27,255</u></u>





Breakeven Analysis

As you learned in Chapter 5, breakeven analysis is a useful tool for determining how increases in sales will affect your profits. The breakeven point is the volume of sales that must be made to cover all of the expenses of a business. Below the breakeven point, your expenses will exceed your revenues and you will be losing money. Once you reach the breakeven point, your sales will equal all of your expenses. This means that at this level of sales, you will neither make nor lose money. Once you exceed the breakeven point, you will begin to earn profits as shown in the graph.

Checkpoint

Why is it important for an entrepreneur to analyze the financial statements of the business?

10.3 Assessment

THINK ABOUT IT

1. How will constructing a cash budget using an electronic spreadsheet make this financial report more helpful?
2. What would be the benefit of preparing an income statement monthly instead of once a year?
3. Which goals do you think are more important to meet: sales goals or profit goals? Explain your answer.

MAKE ACADEMIC CONNECTIONS

4. **PROBLEM SOLVING** If your business were experiencing a negative cash flow, how might you use the six-step problem-solving model to help you?
5. **MATH** Using the Activity CD, open the activity "Cash Budget." Print a copy and complete the activity by preparing a cash budget for your school store and determining ways to increase cash flow.



TEAMWORK

Working in a small group, use the Internet or library to locate a copy of an annual report for a business. Review all of the financial statements that are included in the annual report. Write a paragraph describing the financial statements you have reviewed and include an analysis of the financial condition of the business.



Sharpen Your Entrepreneurial Skills

Leadership Skills

As an entrepreneur and a manager, you need to demonstrate good leadership skills. If you want your business to grow, you must be able to lead and influence others to help you carry out your business vision. A manager who can get individual employees and groups to work well together to accomplish objectives is considered to be an effective leader.

Being a good leader is more than just being nice to people. Characteristics of effective leaders include the following:

1. **Understanding** Respect the feelings and needs of fellow workers.
2. **Initiative** Have the ambition and motivation to see a project through to the end.
3. **Dependability** Follow through on commitments made to employees.
4. **Judgment** Make decisions carefully, objectively, and fairly.
5. **Objectivity** Look at all sides of an issue before making a decision.
6. **Confidence** Make decisions and take responsibility for the results.
7. **Consistency** Do not be too emotional or unpredictable.
8. **Cooperation** Work well with others.
9. **Honesty** Behave ethically and be truthful.
10. **Courage** Be willing to take reasonable risks and make unpopular decisions.
11. **Communication** Listen, speak, and write effectively.
12. **Intelligence** Have the knowledge, understanding, and skills needed to perform well.



© Digital Vision/Getty Images

TRY IT OUT

Leadership styles vary from person to person. Choose two individuals who have played leadership roles in history and research their leadership styles. Prepare a report that illustrates how they exhibited each of the characteristics described above.

Chapter 10 | Assessment

SUMMARY

10.1 Operating Procedures

1. When entrepreneurs become managers, they must utilize a different set of skills. Managers are responsible for planning, organizing, staffing, implementing, and controlling the operations of a business.
2. A detailed operations manual is essential for a business's success. It should include rules, policies, and procedures. Policies may include operating policies, customer service policies, delivery policies, and safety policies.

10.2 Inventory Management

3. A purchasing plan will assist with inventory management by ensuring you have items in stock when they are needed. It helps you calculate ending inventory needs based on beginning inventory, purchases, and sales.
4. You can track inventory using the perpetual or periodic inventory methods. The perpetual inventory method tracks inventory levels on a daily basis. The periodic inventory method involves taking a physical count of merchandise at weekly or monthly intervals.
5. The level of inventory you keep in stock depends on three factors: the costs of carrying inventory, the costs of losing sales due to stockouts, and your stock turnover rate.

10.3 Financial Management

6. To manage cash flow, begin by creating a cash budget. If cash receipts are less than cash disbursements, you will need to improve your cash flow. You can increase cash receipts by offering credit customers discounts for prompt payment, establishing tighter credit policies, establishing a follow-up system for collecting unpaid accounts receivable, and obtaining additional capital for your business. You can decrease cash disbursements by gaining better control over inventory and payroll, slowing the rate at which you pay your bills, and reducing your expenses.
7. When starting a business, you prepare pro forma statements based on projections. Once your business is operating, you will prepare financial statements based on actual performance. The three financial statements most commonly prepared by businesses are the balance sheet, income statement, and cash flows statement.
8. Analyzing financial statements can help you understand how well your business is doing. You can examine your finances by analyzing your sales by product, calculating your net profit on sales, and performing a breakeven analysis.

What do you know now?

Read Ideas in Action on page 269 again. Then answer the questions a second time. How have your responses changed?

VOCABULARY BUILDER

Match each statement with the term that best defines it. Some terms may not be used.

1. The process of achieving goals by establishing operating procedures that make effective use of people and other resources
2. The rate at which inventory of a product is sold and replaced with new inventory
3. A management style in which the manager is directive and controlling
4. The dollar amount of all sales with any returns subtracted
5. A plan that shows how the various jobs in a company relate to one another
6. Keeps track of inventory levels on a daily basis
7. Involves taking a physical count of your merchandise at regular intervals, such as weekly or monthly
8. A management style in which employees are involved in decision making
9. Shows the projections of your cash coming in and going out
10. Contains all of the rules, policies, and procedures that a business should follow in order to function effectively
11. A system that updates inventory records as each sale happens
12. The person responsible for planning, organizing, staffing, implementing, and controlling the operations of a business

- a. authoritative management
- b. cash budget
- c. democratic management
- d. gross sales
- e. management
- f. manager
- g. net sales
- h. operations manual
- i. organizational structure
- j. periodic inventory method
- k. perpetual inventory method
- l. point-of-sale (POS) software system
- m. stock card
- n. stock turnover rate

REVIEW YOUR KNOWLEDGE

13. Which of the following functions of management would apply when grouping tasks into departments?
 - a. planning
 - b. organizing
 - c. implementing
 - d. controlling
14. Jorge is supervising new employees with no experience in food service at a concession stand in an amusement park. Which management style should he use?
 - a. authoritative management
 - b. democratic management
 - c. mixed management
 - d. participatory management
15. **True or False?** The organizational structure outlines all of the rules, policies, and procedures that a business must follow.
16. Preparing detailed plans that will provide strategies for achieving goals and objectives in a one-year period is
 - a. strategic planning
 - b. intermediate-range planning
 - c. short-term planning
 - d. none of the above

17. A small specialty store that has a very limited inventory is more likely to use the ___?___ inventory method.
18. The level of inventory you keep in stock depends on all *except*
 - a. the costs of carrying inventory
 - b. the costs of lost sales due to stockouts
 - c. your stock turnover rate
 - d. your net-profit-on-sales ratio
19. **True or False?** A point-of-sale inventory system makes it easier to analyze your inventory records at the end of the day.
20. **True or False?** Generally, employees do not like to be involved in the planning and decision-making process.
21. If you want to improve your cash flow by increasing cash receipts, which of the following strategies could you try?
 - a. offer discounts on bills paid right away
 - b. establish tighter credit policies
 - c. hold shipments to customers with large unpaid bills
 - d. all of the above

APPLY WHAT YOU LEARNED

22. You received a \$500 payment from one of your customers in the form of a check. You deposited the check into your bank account. Several days later, you received a notice from your bank that the check was returned because your customer's checking account did not have the funds to cover it. You were counting on that money to help you cover your monthly rent. What will you do?
23. You want to analyze your sales by product for your hardware store. Your total sales are \$140,750. The sales of each department in your store are given below. What percent of sales does each department generate for your store?

Seasonal merchandise	\$25,525
Lumber	40,211
Tools	38,524
Lighting	15,235
Kitchen cabinets	21,255

MAKE ACADEMIC CONNECTIONS

24. **MATH** You own a bookstore. The stock turnover rate in the bookstore business is four. How many months worth of inventory must you keep on hand?
25. **COMMUNICATION** You and a partner own a kitchen equipment store. You would like to implement a point-of-sale inventory system using a computerized cash register, but your partner is not convinced this is the best method for your business. Write a letter to persuade your partner to implement a new POS inventory system. Identify advantages of using a POS system.
26. **MATH** You own a pet-supply business. Last year, you sold \$42,000 in dog food and \$53,000 in cat food. Returns totaled \$5,000. The cost of goods sold on the dog food was \$13,000, and the cost of goods sold on the cat food was \$14,000.

Operating expenses for the business were \$13,000 for salaries, \$4,500 for rent, \$1,200 for insurance, \$1,000 for utilities, \$900 for advertising, and \$600 for other. Taxes were \$10,500. What is your net income after taxes? What is your net-profit-on-sales ratio?

27. **PROBLEM SOLVING** Managers are faced with decisions to be made in all areas of business operation. Using the Activity CD, open the activity “Management Problem Solving.” Print a copy and work with a partner to come up with solutions for Katrina’s management issues.



WHAT WOULD YOU DO?



You asked two of your employees to work extra hours over the weekend to perform a physical inventory. You are certain that there were three plasma television sets in stock prior to having the employees take inventory. However, when the inventory was completed, the list showed only two plasma television sets in stock. You checked the stockroom, and you found only two. You have always trusted your employees. What would you do? Will you confront the employees? If so, how will you approach them? Working with a partner, role play the conversations you will have with the employees.

BUILD YOUR Business Plan *Project*

This activity will help you plan the operations management of your business.

1. Describe the management style you will use for managing your business. Will you always use the same style? How will you determine when to use a different style?
2. Locate and contact two professionals in your area who specialize in strategic planning. What are their credentials? What are their fees? Do you think it would be helpful to utilize the services of a strategic planner? Why or why not?
3. Develop an operating procedures manual for your business. Include the rules, policies, and procedures that your business will follow to run effectively.
4. If your business has an inventory, list all of the items you will have in inventory and your cost for each. Create a purchasing plan for your inventory.
5. Set up inventory records for your business using either a paper system or an electronic system. Be sure to list all of the items discussed in Lesson 10.2. How did you determine your reorder point? What inventory carrying costs are relevant to your business? How can you reduce your carrying costs?
6. Analyze your sales by creating a table that lists each of your products and the total sales (or estimated sales) for each. What is the percentage of total sales for each product? Based on this information, will you make any changes to your inventory?

Planning a Career in Information Technology



"My stepsister, who is a high school senior this year, has become our household computer expert. She recently attended a summer technology camp sponsored by a national computer retailer that provides a variety of computer support services. The camp was established as a way to help fulfill future labor needs. After completing camp, she's become the household 'go to' person for any high-tech gadget issues."

How do individuals and small businesses solve computer-related technology problems?

Computer service specialists, who make on-site visits to homes and businesses, help resolve a variety of complex technological issues that affect computer efficiency and reliability. As computers and personal gadgets have become more complex, the need for these service specialists has increased.

EMPLOYMENT OUTLOOK

- Faster than average growth is anticipated.
- The continued expansion of highly sophisticated mobile devices will help fuel demand.
- Growing demand for computer specialists will be somewhat offset by the trend to outsource computer support to foreign countries with lower labor costs.

JOB TITLES

- Software Support Specialist
- Help Desk Analyst
- Application Specialist
- Technical Support Associate
- MIS Support Technician

NEEDED SKILLS

- Degree requirements vary between an Associates Degree

and a Bachelor's Degree in computer-related areas.

- Sometimes relevant computer experience or professional certification can serve in lieu of a degree.
- Strong analytical, problem-solving and interpersonal skills are needed to resolve technical issues among a wide user group.

What's it like to work in Information Technology

Milo is a self-employed PC service specialist who helps his customers solve their computer problems.

Today, Milo is updating the rates on his company web site. These rates include the trip charge to arrive at a client's home or place of business, the one-hour minimum labor charge, and the additional fees for a partial hour beyond the one-hour minimum.

After receiving a call from a frantic client, Milo dashes off to the client's home. The client, who has a home-based consulting business, has a hard drive that is failing. Because the client had accidentally dropped his flash drive in a cup of coffee, he had no backup for his files. Consequently, he needed help retrieving critical files from his hard drive.

After saving the files to a new flash drive, Milo suggests to his client that he consider investing in an automated data backup service. For a monthly fee, designated data would be automatically saved to a personalized web site that would be password accessible for security purposes.

What about you? Would you like to help a variety of individuals and businesses solve their computer technology problems?



PARTNERSHIP WITH BUSINESS

The Partnership with Business Project is based upon developing and implementing the most innovative, creative, and effective partnerships between the FBLA chapter and businesses. The purpose of this project is to learn about a business through communication and interaction with the business community. This project can be completed by one to three students.

A report will be prepared that describes activities designed to bring business leaders and FBLA members together in a positive working relationship through innovative programs. The event should not involve fundraising for the FBLA chapter. The report should include the following sections: Development (description of the partnership goals, description of planning activities used to build a partnership, roles of business leaders and chapter members in developing the partnership); Implementation (description of activities, level of involvement from business leaders, roles of business leaders and chapter members); Results (description of concepts learned from the project and the impact of the project); Degree of Involvement (hours spent and contacts made); and Evidence of Publicity (description of the recognition received as a result of the partnership). Participating teams will be given seven minutes for oral presentations to describe the project and the results. The judge has three minutes to ask questions about the presentation.

PERFORMANCE INDICATORS EVALUATED

- Develop a partnership with business by describing partnership goals, planning activities, and roles of business and FBLA leaders.
- Implement the project by describing activities, defining roles of participants, and encouraging involvement from business leaders.
- Describe the results from the business partnership project.
- Acquire knowledge of business operation by implementing an active business partnership.
- Develop a stronger understanding and relationship between school and the business community.

Go to the FBLA web site for more detailed information.

Think Critically

1. How can a business benefit from participating in the partnership?
2. How can the FBLA chapter benefit from the partnership?
3. Why is publicity so important for this project?
4. What is one strategy that could be used to increase involvement of more businesses in this project?

www.fbla.org

Chapter 11

© Digital Vision/Getty Images



Human Resource Management

11.1 Identify Your Staffing Needs

11.2 Staff Your Business

11.3 Direct and Control Human Resources

school.cengage.com/entrepreneur/ideas

IDEAS IN ACTION

Working for What You Believe In

In 1997, when Omar Faruk was 9 years old, he emigrated with his family from Bangladesh to the United States. He started working after school to earn money for clothes and school trips. At age 14, he started his first business as a web site offering one product for sale. The business did not turn out to be very successful for Omar, but he gained experience in setting up the web site. Omar knew that there were many potential customers who could use his web skills.

While a senior at Independence High School in New York City, Omar started building web sites for nonprofit organizations, and his business, Blue-Stream, was born. Omar won several awards for his business, including the National Foundation for Teaching Entrepreneurship's 2006 Entrepreneur of the Year, Bank of America's Young Entrepreneur of the Year, and Ernst & Young's Entrepreneur of the Year, of which he became the youngest recipient.

Omar has a strong interest in social causes and now operates his business under the name LogicLotus. LogicLotus is focused on providing services for nonprofits, social causes, and small businesses. He began with a business plan but today manages his business through experiences and trying out new ideas.

Today, Omar employs two individuals to assist him. He has found some challenges in managing younger workers but feels that they are willing to help carry out his vision for the business. He uses profit sharing as the method of paying the employees, so the harder they work, the more they earn.

Omar realizes that the key to growth is selling. Dreams are important, but you have to take a good look at what you do and sell it to others.

Omar's "top tips" for aspiring entrepreneurs are as follows:

- Failure is part of the process. Take life as an opportunity.
- Don't be afraid to ask for help. There are many people and organizations willing to help you.
- Always carry paper and pen—ideas don't just come one at a time!



© Omar Faruk

Omar Faruk, LogicLotus

What do you know?

1. Although Omar started with a business plan, he does not use one now. Do you think it would help Omar to have a current business plan?
2. Do you think paying employees with a profit sharing plan is an effective payment method?
3. What do you think of Omar's top tips?

11.1 Identify Your Staffing Needs

Goals

- Explain how to determine staffing needs for a business.
- Describe options for recruiting employees.
- Identify alternatives to hiring permanent employees.

Terms

- staffing
- job description
- job analysis
- chain of command
- recruit
- freelancers
- interns

Focus on Small Business

Help wanted

Emanuelle started his contracting business six months ago. He specialized in bobcat work and had more business than he could handle. He decided he needed help and posted a “Help Wanted” sign along with his phone number in front of his business. People began calling and stopping by, continually interrupting his work. They wanted to know what type of work he had and how much it would pay. Emanuelle didn’t really know what to tell them. He had not thought through the details of the posted position.

In his business, Emanuelle had a large amount of paperwork to do and more bobcat work than he could keep up with. He realized that if he had help with the administrative tasks, he would have more time to devote to the bobcat work. But he could also use someone else with bobcat experience to help out as well. Emanuelle took down his sign to determine exactly what type of help he needed.

Work as a Team What do you think Emanuelle should have done before posting the “Help Wanted” sign? What types of positions could Emanuelle add? Do you think using a sign in front of his business is the best way for Emanuelle to attract qualified job applicants?



© PhotoDisc/Getty Images

Think through your staffing needs before posting a help wanted sign.

Staffing

The management functions of staffing, implementing, and controlling can be directly applied to the people who work for your business. The people who work for your business are your *human resources*. You may not need to hire employees when you first start your business. But as your business grows, you will find the need for employees. Good employees and a well-run human resource management program are as important to your business as are capital, equipment, and inventory.

Staffing involves determining the number of employees you need and defining a process for hiring them. To find out your staffing needs, ask yourself these questions:

- What kind of employees do I need?
- What skills am I missing?
- What skills do I need daily?
- What skills do I need occasionally?

To answer these questions, list all the duties in your business. Then try to identify how much time is needed to perform each of these duties. Your list should help you identify whether you need part-time, full-time, or temporary workers. You can also determine whether you need managers or assistants and how many employees you need.



© PhotoDisc/Getty Images

What staffing needs might a hair salon have?

★ Develop Your Reading Skills

Make an interactive notebook for this chapter. Before you read, divide your paper into two columns. In the left-hand column record notes about what you are reading. In the right-hand column, write notes that will help you relate what you are reading to your everyday life.

Job Descriptions

A *job* is a collection of tasks and duties that an employee is responsible for completing. A *task* is a specific work activity that is performed, such as answering the telephone or answering e-mail. Many positions include a variety of tasks that are sometimes referred to as *functions*. A **job description** is a written statement listing the tasks and responsibilities of a position. Job descriptions also include to whom the position reports, educational and professional experience required, and salary range.

Job descriptions are written after conducting a **job analysis**, which is the process of determining the tasks and sequence of tasks necessary to

SAMPLE JOB DESCRIPTION

Title: Account Executive

Tasks and Responsibilities: Plans, coordinates, and directs advertising campaigns for clients of advertising agency. Works with client to determine advertising requirements and budgetary limitations. Coordinates activities of workers engaged in marketing research, writing copy, laying out artwork, purchasing media time and space, developing special displays and promotional items, and performing other media-production activities.

Qualifications: College degree with courses in marketing, leadership, communication, business, and advertising; sales experience; interpersonal and written communication skills; neat professional appearance; characteristics of self-motivation, organization, persistence, and independence

Reports to: Marketing Manager

Salary Range: \$30,000 to \$50,000, depending on experience



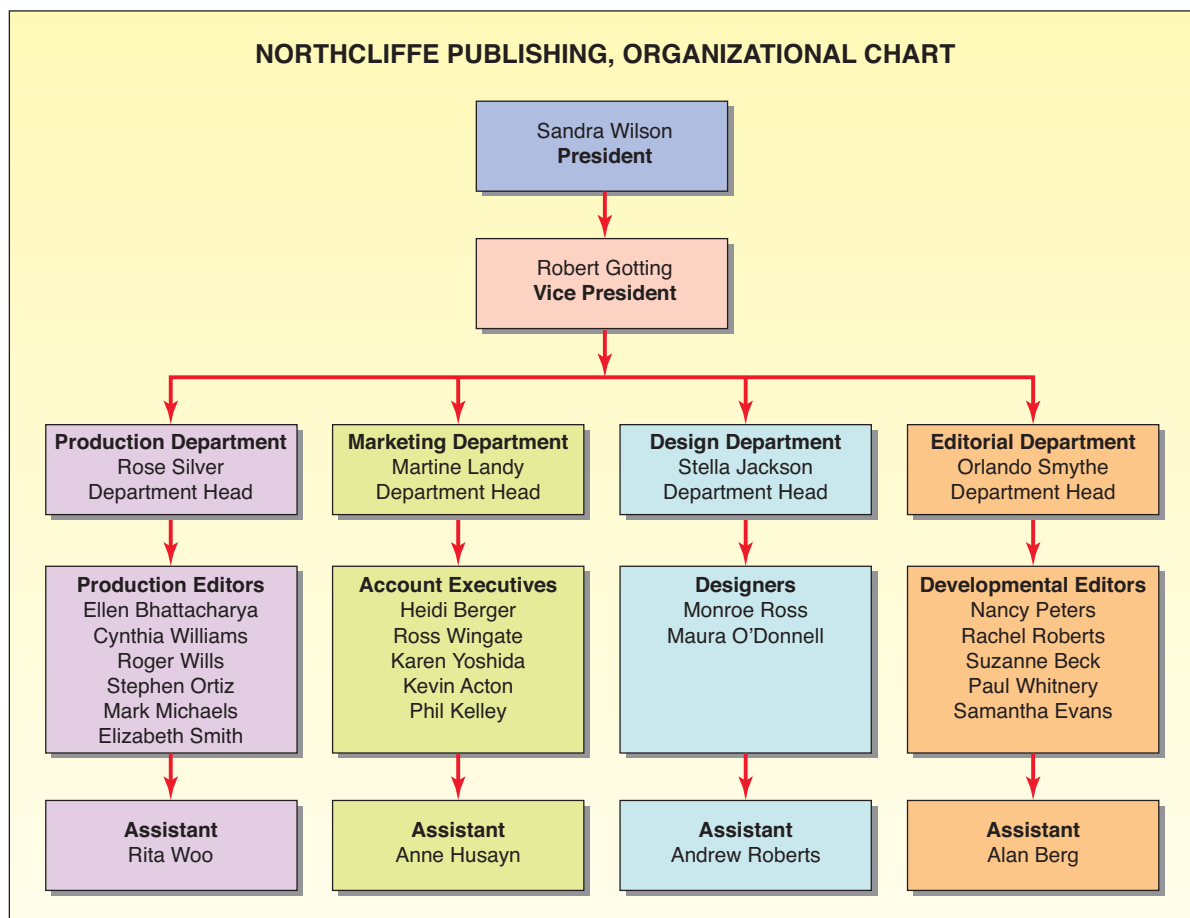
perform a job. You will need to understand exactly what every job involves so that you can determine how much money to offer job applicants. A detailed job description will make clear the job responsibilities. If a sales assistant objects to answering phones, you can refer that employee to the job description that lists this task as part of the job. Job descriptions also can be used to measure how well an employee performs a job.

Organizational Structure

Once your company has several employees, you will need an organizational structure. An *organizational structure* is a plan that shows how the various jobs in a company relate to one another. Many businesses use a chart to represent the organizational structure. The organizational chart can also help you analyze your staffing needs. Using the chart during planning can help you identify the number and types of employees you need. When planning, you can list positions and primary responsibilities of each. Then as employees are hired, you can fill in the names.

The organizational chart shows who reports to whom in the company, or the **chain of command**. In a small business, all employees may report directly to the company owner. In large companies, lower-level employees usually report to a supervisor. This kind of organizational structure ensures that the owner is not called upon to deal with relatively unimportant issues that could be handled more efficiently by a lower-level manager.

Sandra Wilson owns Northcliffe Publishing. Sandra has an organizational structure where the heads of the four departments report to





© PhotoDisc/Getty Images

Do you think a want ad in a newspaper is a good way to find job candidates? Why or why not?

the vice president, Robert Gotting. Robert in turn reports directly to Sandra. This structure helps Sandra devote her time to long-term issues, such as expanding the company into new areas or increasing sales and market share.

Checkpoint

How do you determine staffing needs for your business?

Recruiting

To **recruit** is to look for people to hire and attract them to the business. As the owner of a small business, it may be difficult for you to attract experienced employees to work for your business. They may have opportunities to work for larger, established businesses that can offer them higher pay and better benefits. You can use a variety of resources for recruiting, including classified advertisements, online career and employment sites, employment agencies, college placement centers, in-store advertising, and referrals.

Classified Advertisements

Using the local newspaper for advertising is a good way to attract a large number of applicants. The advertisement that you place in the newspaper is called a *want ad*. It should briefly describe the position and the education and experience requirements. It should also identify any special job requirements, such as willingness to travel or to work evenings. You should request resumes and cover letters from applicants interested in the position. Sometimes employers ask for specific information in the cover letter, such as salary requirements, date of availability, or other useful information. If you do not want to give the name of your business in the ad, newspapers have PO boxes to which applications can be sent. You should screen the resumes to determine which applicants you want to interview.





© PhotoDisc/Getty Images

Why are online career web sites becoming a popular way to recruit employees?

Online Career and Employment Sites

Many people now use the Internet to look for a job, so many employers are advertising with online career and employment sites. Most online employment services allow you to post a job and then search the resumes that are sent in response to the posting. Some online employment services have a database of resumes that you can review when you are looking for someone to fill a specific job. According to Monster.com, job seekers post over 27,000 new resumes and conduct 3.9 million job searches on its site every day. Online recruiting can be very expensive, so you should compare alternatives and be sure that this is the best method for your business.

Employment Agencies

Employment agencies find employees for businesses and other institutions. These firms try to match people looking for jobs with businesses looking for employees. They charge businesses and/or the job seekers

a fee when they are successful in making a match. Seeking applicants through an employment agency saves time for the employer in screening applicants, but the cost is higher than a classified advertisement.

College Placement Centers

Most colleges and universities operate job placement centers. These offices collect information on career and employment opportunities, which they make available to their students and graduates. Generally, they do not charge a fee for their services. If college students or graduate students might be suitable for your business, contact local colleges and universities and ask them what you need to do to have your business listed with their placement center.

NETBookmark

Manpower, Inc., provides workforce management services to customers through 4,400 offices in 73 countries. The firm annually provides employment to more than 4 million people. Access school.cengage.com/entrepreneur/ideas and click on the link for Chapter 11 to learn more about Manpower's services. Why might a small business owner turn to companies like Manpower to recruit employees? Name one possible drawback a small entrepreneur might face when using an employment agency for recruiting.

school.cengage.com/entrepreneur/ideas

In-Store Advertising

Have you ever walked into a store and seen a sign that says “Help Wanted” or “Now Hiring”? This is another method of recruiting that businesses use. When you post a sign, interested applicants will come into your business and fill out an application form. Before placing a sign in the window, be sure you will have time to deal with the many people who may stop to inquire about the position. You can interview them at that time or set up an interview at another time. If you interview everyone who comes in, you need to realize that this will be very time-consuming.

Referrals

One of the best ways entrepreneurs find employees is by acting on referrals from friends, acquaintances, or employees. If you consider the person making the recommendation reliable, a referral may require very little screening. However, many business owners do not like to hire friends or relatives of current employees because it can sometimes create other problems.

Checkpoint

What resources can you use for recruiting employees?

Alternatives to Adding Staff

Adding employees to your payroll is costly. It takes time and money to recruit staff and to track, report, and pay their salaries, benefits, and tax withholdings. In many cases, you may need help but not have sufficient work to keep a permanent, full-time employee busy. For these reasons, you may want to consider alternatives to permanent employees, such as hiring freelancers, interns, and temporary workers.

Freelancers

Freelancers are people who provide specialty services to businesses on an hourly basis or by the job. Examples of freelancers include bookkeepers, accountants, lawyers, graphic designers, window display artists, and advertising copywriters. Business owners use freelancers when they need to have a job done but do not have enough of the required type of work to warrant hiring a permanent employee.

Interns

Interns are students who will work for little or no pay in order to gain experience in a particular field. To find out whether interns are available in your community, contact local colleges and high schools. If you hire an intern, you will most likely have to work with a college or high school intern coordinator to ensure certain program requirements are fulfilled. It is your responsibility to provide a valuable learning experience for the intern.



Temporary Workers

Businesses that need additional help often use temporary workers. Some temporary workers are seasonal employees. Other temporary workers are substitutes for employees who are sick or on a leave of absence. Temporary employment agencies provide trained workers for various kinds of businesses. A business that uses a temporary employee pays a fee to the agency. The agency in turn manages the worker's salary and benefits.



© PhotoDisc/Getty Images

Why would a business hire a temporary worker?

Checkpoint

What are some alternatives to hiring permanent employees?

11.1 Assessment

THINK ABOUT IT

1. Why is it important for a company to have an organizational structure that allows the owner to focus on long-term issues?
2. List some advantages of using an employment agency.
3. What would be some disadvantages of hiring freelancers and temporary workers?

MAKE ACADEMIC CONNECTIONS

4. **PROBLEM SOLVING** Create an organizational structure for a 30-person local package delivery service. First, determine all the types of employees the business would have. Then create the chart based on your decisions.
5. **RESEARCH** Create a resource guide containing online career and employment web sites, employment agencies, and college placement centers that could be used to help meet staffing needs. Include contact information for each resource.



TEAMWORK

Form teams. Choose a business in your community. Decide what the best method would be for it to recruit new employees. Design an advertisement that could be used for the method you select. If you select referrals as the best method, design a referral request form that could be sent to friends, acquaintances, and current employees.

11.2 Staff Your Business

Goals

- List and describe the steps in the hiring process.
- Describe compensation packages for employees.
- Identify laws protecting employee rights.

Terms

- wages
- salary
- bonus
- profit sharing
- commission
- benefits

Focus on Small Business

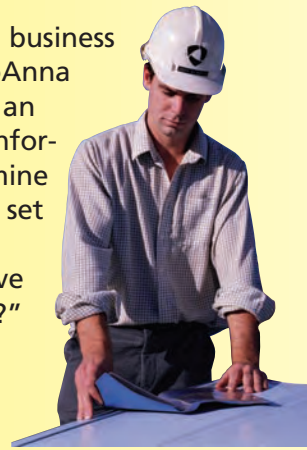
Whom to hire?

Emanuelle took a good look at his business needs and decided that he would hire an administrative assistant to help him. If he had someone in the office to answer the phone, schedule work, and handle the billing, it would allow him to spend more time at job sites. He put an ad in the local newspaper and had several candidates contact him. Now he had to decide who to interview.

Emanuelle's sister, JoAnna, had run her own business for several years, so he went to her for advice. JoAnna recommended that he have candidates complete an application form. He could review the provided information and check with their references to determine who is really qualified for the job. Then he could set up interviews with the best candidates.

"So, JoAnna," Emanuelle asked, "do you have an application form lying around here anywhere?"

Work as a Team Do you think that JoAnna gave Emanuelle good advice about selecting candidates to interview? Why do you think it is important to review and verify the information that applicants provide?



© PhotoDisc/Getty Images

Consider the skills needed to improve your business.

The Hiring Process

Hiring employees is often difficult because it requires making very important decisions based on fairly limited information. How should you decide whom to hire? The four-step hiring process involves (1) screening candidates, (2) reviewing and verifying job applications, (3) interviewing the best candidates, and (4) making a job offer.

Screen Candidates

The first step in the hiring process is to screen candidates to remove people who are not right for the job. This allows you to focus on the most qualified candidates. The job description identifies the specific requirements needed to perform a particular job. You need to match the job candidate's

experience and skills with the job description. You should also look for personal characteristics that would make a person a desirable employee.

Michael Johnson, owner of Johnson's Medical Supply, ran a want ad in the local newspaper. He was looking for a person with at least five years of experience selling medical equipment. He received more than 150 responses to his ad. However, 120 of the resumes he received were from people with no experience in the field. Michael immediately removed those from the stack of possibilities. Next, he carefully examined each resume and cover letter and selected ten candidates to interview based on their experience.

Review and Verify Job Applications

You will need to have potential candidates complete an application. There are standard application forms that you can use, or you can design one that will meet your specific needs. The application allows you to gather information that might not be included on a resume. If you decide to design your own application, you can use the job description as a guide to gather the information you need about the candidate's experience.

Once you have applications and resumes from candidates, you need to verify that the information provided is correct. The first thing you should do is check references. Call previous employers to make sure the applicant held the positions listed on the resume. Ask what they can tell you about the person. Describe the job opening, and ask the previous employers if the candidate would perform well in such a position. Other questions can revolve around the personal qualities of the candidate, such as interpersonal skills and punctuality. Request that the candidate provide an official transcript from schools they attended to verify education and training.

Interview the Best Candidates

The job interview provides you with the opportunity to determine whether a prospective employee would improve your ability to meet customer needs. It is also your chance to make your small business appealing to a prospective employee. Making the most of the job interview is as important for you as it is for the job candidate.

SELL YOUR BUSINESS During the interview, make your small business appear inviting and appealing to prospective employees.

- **Share your values and plans for the business.** Help the applicant understand your vision for the business.
- **Talk about the significance of working in a new business.** Emphasize the importance of the contributions the applicant would make in the development and growth of a new business.
- **Explain the atmosphere in which the candidate would work.** Make sure the applicant understands that a small business can foster an environment of flexibility and caring. Some people would rather work in a small business that is not as structured as a large corporation.
- **Describe your bonus system.** With a small startup business, you may not be able to pay a large salary, but you can offer an attractive



bonus or benefits package. Explain that if the business does well, you will share some of the profits with those who help you succeed.

MAKE THE INTERVIEW EFFECTIVE

To ensure that you use your time during the interview effectively, follow these basic rules:

1. **Be prepared.** Make a list of open-ended questions you want to ask. Review the job candidate's resume and application again just before the interview begins.
2. **Be courteous.** Do not be late for the interview. Avoid taking phone calls during the interview. Try to put job candidates at ease by offering them something to drink. Make them feel welcome in your office.
3. **Avoid dominating the interview.** Remember that the interview is your opportunity to get to know the job candidate. To do so, be sure to allow the applicant plenty of time to speak.
4. **Take notes.** Throughout the interview, jot down your impressions of the candidate as well as any interesting information he or she reveals.
5. **Look for warning signs.** Signs that a person may not be a good worker include frequent job changes, unexplained gaps in employment, and critical comments about previous employers.
6. **Don't make snap judgments.** Don't rule out a candidate until the interview is over.
7. **Remain pleasant and positive throughout the interview.** At the end of the interview, thank the candidate for coming and let him or her know when you plan to make a decision.
8. **Write a summary of your impressions of the candidate.** Write your summary immediately after the interview while your thoughts are still fresh. Put this document in the candidate's file.

SAMPLE INTERVIEW QUESTIONS

1. What interests you about the job?
2. How can your skills and experience benefit the company?
3. What are your career plans? How does this job fit in with those plans?
4. What other positions have you held? What did you like and dislike about those positions?
5. What were your achievements at your previous jobs?
6. Why did you leave your last job?
7. How do you think your education has prepared you for this job?
8. What kind of work do you enjoy most? What makes a job enjoyable for you?
9. Describe a situation where you had to manage conflicting priorities.

Make a Job Offer

When you have decided to make a job offer, contact the person by phone. Let the person know you were impressed with his or her credentials. Be sure to emphasize how much you would like the applicant to join your company. Clearly state the starting salary, benefits, and terms of employment. If the first applicant declines your offer, extend the offer to your second choice and then to your third choice, if necessary.

Once a candidate accepts your offer, contact the remaining candidates. Thank them for interviewing with your business, and politely let them know that you have given the job to another applicant.



Checkpoint

What are the four steps in the hiring process?

Compensation Package

As an entrepreneur with paid employees, you will need to create a compensation package. The package will include some type of pay and may also provide a variety of benefits. The benefits package can influence a candidate's decision on whether or not to take a position with a company.



© Digital Vision/Getty Images

Why are many salespeople paid using a commission plan?

Types of Pay

There are many ways you can choose to pay your employees. The terms “wages” and “salary” are often used interchangeably, but there is a difference. **Wages** are payments for labor or services that are made on an hourly, daily, or per-unit basis. The paycheck for a person earning a wage will vary depending on how many hours are worked or how many units are manufactured. A **salary** is an amount paid for a job position stated on an annual basis. Regardless of the number of hours the person filling the position works, the amount of money the salaried employee is paid does not vary. Wages and salaries can be paid weekly, biweekly, or monthly. Employees may also receive a **bonus**, which is a financial reward made in addition to a regular wage or salary. Bonuses usually hinge on reaching an established goal. **Profit sharing**

is another compensation arrangement in which employees are paid a portion of the company's profits.

Some employees are on commission-based salary plans. A **commission** is a percentage of a sale paid to a salesperson. A commission-based salary varies from month to month depending on sales. Those receiving this type of salary may be paid using a commission-only plan or a combination plan.

COMMISSION-ONLY PLAN Some employees, especially those in sales, receive all of their salaries in commission. Commission-only plans are good for employers, because commissions are paid only when sales are made. Some employees may not want to accept a commission-only position, because they are not comfortable with the uncertainty of not knowing what their actual pay will be from pay period to pay period.

Lyn Kovacs works entirely on commission. Last year, Lyn sold \$490,000 worth of electronic devices. She received ten percent of her sales as commission. Her annual salary was \$49,000, as calculated below.

$$\begin{array}{rclclcl} \text{Amount sold} & \times & \text{Percent of commission} & = & \text{Amount of commission} \\ \$490,000 & \times & 0.10 & = & \$49,000 \end{array}$$

COMBINATION PLAN An employee may be paid based on a combination plan. A combination plan includes a base salary plus commission. Employees may feel more comfortable accepting a position that offers this type of payment plan.

Hector Marquez sells men's clothing at a local department store. He earns \$6.75 an hour, plus ten percent of whatever he sells. Last month, Hector worked 158 hours and sold \$11,500 worth of clothing. His total monthly compensation was \$2,216.50, calculated as follows:

Base Pay	+	Commission	=	Total Pay
(Hours × Hourly wage)	+	(10% × Sales)	=	Total Pay
(158 × \$6.75)	+	(0.10 × \$11,500)	=	Total Pay
\$1,066.50	+	\$1,150.00	=	\$2,216.50

PAY COMPETITIVELY In most markets, wages and salaries are competitively determined. This means that an employer who offers much less than the going wage or salary rate is not likely to find qualified workers. To offer competitive wages or salaries, you will have to find out how much similar businesses in your area are paying their employees. You should also find out what people are earning in jobs with similar qualifications. Once you know the going wage or salary rate, you will have to decide whether you want to offer more than, less than, or about the same as other businesses. Offering more than other businesses will attract the best employees.

Bob Aylward owns a limousine service. He knows that finding and keeping good drivers is difficult. To make sure his compensation package is attractive, he regularly finds out what other limousine companies are offering. He then sets a starting salary that is three percent higher. He also offers a few more days of paid vacation than his competitors. Bob hopes that these things will attract drivers that will stay with his company for many years.

Benefits

Benefits are employment rewards for service in addition to salary. They may include paid leave, insurance, and a pension plan.

PAID LEAVE Almost all employers offer paid vacation and sick time. Both kinds of leave represent costs to employers, because employees are paid while they are not working. Be aware that some employees may abuse paid leave. You or someone in your business should keep a record of the paid leave employees take and watch for patterns that might indicate abuse.

Businesses handle vacation in various ways. Many offer one or two weeks of paid vacation a year to new employees. Employees usually gain more vacation time the longer they work at a business. Some businesses let employees carry over unused vacation days from year to year while others require employees to use their vacation time each year.

Sometimes your employees will not be able to work because of illness. The number of days of sick leave provided varies from business to business. Some businesses offer only five sick days a year. Others allow employees unlimited sick leave. You will have to develop a sick leave policy that is fair to your employees but not excessively costly to you.

did you KNOW?

When the minimum wage law was first enacted in 1938, the established minimum wage was just 25 cents per hour.



INSURANCE Many businesses offer health insurance as a benefit to full-time employees. The cost to small businesses to provide insurance coverage can be quite high. Large businesses receive discounted group rates but may still require employees who opt for this benefit to pay a portion of the cost. Businesses may also offer other kinds of insurance such as dental insurance, life insurance, and accident insurance.

RETIREMENT PLANS Some businesses help employees save for retirement by offering 401(k) plans. Employees that participate in 401(k) plans have a percentage of their earned income withheld by the employer to be deposited into a professionally managed investment account. Some employers will match employee's 401(k) contributions as much as 50 cents per dollar invested. The funds will continue to grow tax-free until they are withdrawn by the retiree upon reaching retirement age. Pension plans are another type of employer-sponsored retirement savings plan, but they are not as common because they are more costly to a company.

Checkpoint

What may be included in a compensation package for employees?

Famous Entrepreneur

J. K. Rowling

Ask successful people how to succeed, and they will always tell you to do what you love. For a fortunate few, that formula works. Such is the case with J. K. Rowling, creator of Harry Potter and one of the most successful writers in the world today.

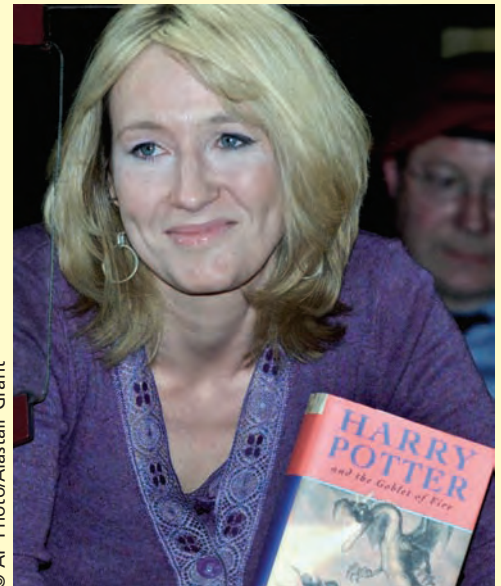
Rowling always wanted to be a writer and eventually became one, but before Harry and success came a young adulthood full of indecision. Her favorite subject in school was English, and she liked studying languages too. Rowling went to Exeter University and studied French. Her parents thought languages would lead to a career as a bilingual secretary. She discovered that she liked nothing about being a secretary and spent time working on stories at the computer when she thought no one was looking. Such misbehavior eventually got her fired, so Rowling went abroad

to teach English as a foreign language in Portugal. With her mornings free, she began work on her third novel after giving up on two others when she realized how bad they were.

When she left Portugal, her suitcase was filled with stories about Harry Potter. She settled in Edinburgh and decided to finish the novel and try to get it published before starting work as a French teacher. A publisher bought the book one year after it was finished. The road to success for J. K. Rowling had begun!

Think Critically

J. K. Rowling found great success as a writer, but her experience as an employee was not very successful. Why do you think this is often the case with entrepreneurs?



© AP Photo/Alastair Grant

What can you learn about entrepreneurship from J. K. Rowling's experiences?

Regulations that Protect Employees

There are many laws designed to prevent discrimination and promote health and safety in relation to employment. It is important to consider these regulations as you develop your staffing plan.

Fair Labor Standards Act (FLSA) of 1938

The FLSA establishes the maximum number of hours employees can work. It includes rules for children under the age of 16 who work and pay rates for overtime work. The act also outlines the national minimum wage.

Civil Rights Act of 1964

Title VII of the Civil Rights Act prohibits discrimination on the basis of race, color, religion, sex, or national origin in hiring, promotion, discharge, pay, fringe benefits, job training, classification, referral, and other aspects of employment. This law is enforced by the Equal Employment Opportunity Commission (EEOC), a government agency established by Congress in 1972 to regulate labor laws.

Age Discrimination in Employment Act of 1967

The purpose of this act is to promote employment of older persons (40 and over) based on their ability rather than their age. It prohibits arbitrary age discrimination in employment and helps employers and workers find ways of resolving issues that arise from the impact of age on employment.

Occupational Safety and Health Act (OSH Act) of 1970

The OSH Act requires that employers maintain safe working conditions for their employees. To comply with the act's regulations, you must keep records that show the steps you have taken to protect the welfare of your workers and to keep your workplace safe. If employees have to work with dangerous equipment or substances, you must provide them with special training. If the Occupational Safety and Health Administration (OSHA) suspects that your business has unsafe practices, its inspectors will examine your facility and may require you to make changes.

Immigration Reform and Control Act of 1986

This act requires that employers check the identification of employees hired after 1986 to ensure that they are legal citizens of the United States. It also established the Office of Special Counsel for Immigration-Related Unfair Employment Practices to enforce antidiscrimination provisions.

Americans with Disabilities Act (ADA) of 1990

The ADA bans discrimination against employees based on disabilities. It requires businesses with 15 or more employees to accommodate the needs of employees with disabilities, even if the firms currently do not have disabled employees. The intent of the ADA is to protect job applicants and employees who are legally disabled but are qualified for a specific job. An employee is qualified if he or she can carry out



the necessary functions of the job with some type of reasonable accommodation.

Family Medical Leave Act of 1993

This act requires businesses with more than 50 employees to provide employees up to three months of unpaid leave if a serious health condition affects the employee, the employee's child, or the employee's parent or spouse. This act also makes it possible for male and female employees to take leave in the event of a birth or adoption of a child.

Checkpoint

Why do we need laws to help protect the rights of employees?

11.2 Assessment

THINK ABOUT IT

1. Why is it important for an employer to check the information and references provided by a job applicant?
2. Why is the compensation package important to potential employees?
3. Why is it important for small business owners to have an understanding of the laws designed to protect employees?

MAKE ACADEMIC CONNECTIONS

4. **RESEARCH** Find and compare three advertisements for the same type of job. Are the qualifications requested the same? How are they different? Is any mention of compensation made? If so, how is it structured? Research the going wage for this position. What do you think is a fair wage for this job?
5. **MATH** You have an open sales position in your company that pays a salary of \$21,000 per year. You discover that another company with a similar sales position offers a combination plan of \$12,000 per year plus a commission of 15 percent of sales. Average sales are \$90,000. Which job has the potential for higher earnings? Do you need to adjust your salary? Why or why not?



TEAMWORK



When interviewing job candidates, there are questions you cannot legally ask. Using the Activity CD, open the activity "What Can You Ask in an Interview?" and print a copy. Working with a partner, review the list of interview question guidelines. Then, think of a position in a company and make a list of interview questions adhering to the guidelines. Role play an interview for the position.

11.3 Direct and Control Human Resources

Goals

- Explain what should be included in the implementation of your staffing plan.
- Discuss ways to motivate your employees.
- Describe the control function of management as it applies to human resources.

Terms

- delegate
- performance evaluation

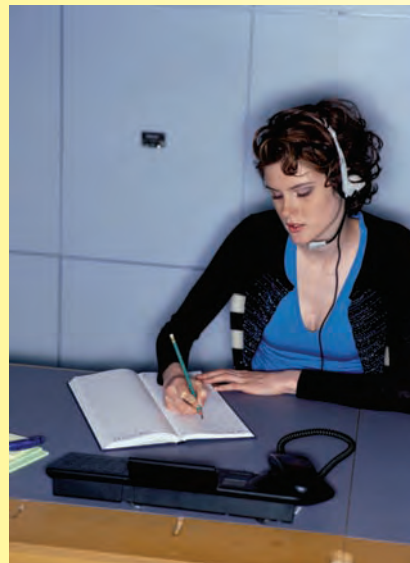
Focus on Small Business

You've hired someone, now what?

Emanuelle carefully screened the applicants for administrative assistant, interviewed a couple of candidates, and offered the position to Vivian. Vivian reported to work bright and early on a Monday morning. Emanuelle reviewed her job description with her, showed her how the phone system worked, and then headed out to do some bobcat work.

He hadn't been gone 20 minutes when his cell phone started ringing. It was Vivian. She was in a panic because she had received several calls about bobcat services. Customers wanted to know the costs and when they could be scheduled for service. Vivian didn't know what to tell them, and some customers became impatient and demanding. Emanuelle quickly turned his truck around and headed back to his shop. On the way there, he tried to figure out what to do.

Work as a Team What mistakes do you think Emanuelle made after hiring Vivian? What does he need to do now?



© PhotoDisc/Getty Images

Well-trained employees help a business succeed.

Implement Your Staffing Plan

Once you have people working for you, you become a manager. This means that you will no longer focus all of your efforts on doing your own job. You will be *implementing*, which involves directing and leading people to accomplish the goals of the organization. As a manager, you will have to exhibit leadership and motivate your employees.

To manage your staff effectively, you need to understand the levels of management and develop good leadership qualities. This will help you create a workforce that is dedicated to meeting customer needs and increasing sales.

Understand the Levels of Management

There are three basic levels of management: supervisory level, middle level, and top-management level. The amount of responsibility varies with the level of management. As the manager moves up, the amount of responsibility increases. The number of managers at each level will vary depending on the size of the company. In a new business venture, the entrepreneur may serve in all levels of management. A large corporation may have many individuals working as middle and supervisory-level managers.

Supervisory-level managers work directly with the workers on the job and are responsible for implementing the plans of middle management. Middle managers serve as a liaison between the supervisory-level and the top-level managers. They are responsible for implementing the goals of top management. Top management has the highest level of responsibility and is responsible for establishing the vision for the company.

Apply Leadership Styles

As you learned in Chapter 10, managers will develop a style or way of working with those whom they supervise. Leadership styles have changed over the years as the workplace has changed. Successful managers today often empower their employees and give them the authority to make decisions without supervisory approval. Empowerment gives employees a sense of responsibility and pride in accomplishment. It also reduces delays in the flow of work and reduces the workload of the manager.

However, not all managers use this style. There are many different leadership styles. Some managers use fear and intimidation and manage their employees as if they are lazy and cannot be trusted.

They are called *Theory X managers* and use the authoritative management style. Other managers trust and respect their employees and value their contributions. They are called *Theory Y managers* and use the democratic management style. Some managers reward employees for good work. In your working career, you will encounter many different leadership styles. When you become a manager, incorporate the qualities you like in other leaders into your leadership style.

Enforce Employee Policies

As the owner of your own business, you will establish policies concerning vacations, holidays, hours, acceptable dress, and other issues affecting your workers. You will need to make sure that all of your employees are familiar with these policies. You may need to gently remind employees of policies if they fail to follow them.

BE YOUR OWN BOSS

You own a floral design studio. Last year, you promoted Philip, one of your designers, to manager of the studio. Philip had shown excellent design skills and was eager to take on new responsibilities. Recently, Philip has become increasingly possessive of information about what is going on in the day-to-day management of the floral shop. Several major problems with important customers have surfaced that Philip knew about but had not shared with you. Business from two of these customers has decreased during the last quarter. Also, several staff members have come to you privately with complaints about Philip's management practices. Tina, who has worked for you for over ten years, is threatening to quit. Use the six-step problem-solving method to determine how you will handle the issues with Philip.

Many companies communicate policies to staff by creating an employee handbook. These handbooks can be just a few pages long or they can fill a small binder, depending on the size of the company and the number of policies.

Train Your Employees

You will need to develop a training program for your new employees. This program should begin as soon as they are hired. Training should not end when the employee learns how things are done. Continuous training ensures that employees are always knowledgeable and up to date on changes affecting the business.

There are many ways to provide training to employees. You may use different techniques for different job responsibilities. You will need to decide which is best for you, your business, and the employee.

- **On-the-job training** Employees learn new responsibilities by actually performing them at their place of business.
- **Coaching** Employees receive feedback and instruction from their manager on a constant basis.
- **Mentoring** One employee teams up with another more experienced employee to learn a job.
- **Conferences and seminars** Employees attend conferences and seminars to learn about new techniques and trends from an expert in the field. These are usually held off-site.

After training, you need to make sure employees are using that training and that the training was effective. Justin Reynolds needs to train his employees on the new computerized inventory system he wants to use. He brings in a representative from the software company to provide a training session. Justin will know the training was effective if employees understand the software and are able to use it.



© PhotoDisc/Getty Images

Why are conferences and seminars valuable training methods?



Checkpoint

What should be included in the implementation of a staffing plan?

Motivate Your Employees

To get the most out of your employees, you will have to motivate them. You can do so in several ways.

1. **Pay employees well.** When employees feel they are compensated well, they will be happier. They will perform to the best of their ability.
2. **Treat employees fairly.** Everyone wants to be treated well. Be sure to treat everyone the same.
3. **Recognize employees for the work they do.** Offer public recognition for a job well done. Praise employees frequently.
4. **Give employees adequate responsibility.** Employees who are allowed to make decisions on their own often work harder. They take pride in the fact that their input makes a difference.

WHAT WENT WRONG ?

Whom Do You Trust?

Sandy Warren formed Motiva International, a sales motivation and consulting company. Sandy felt it was very important to involve her employees in all business operations. At weekly meetings, she shared and discussed confidential company details with the company's 18 employees. Sandy soon learned that there were some things that should not be shared.

The company was experiencing some cash flow problems, and Sandy discussed this with the employees. Employees became concerned that they would not get paid, which distracted them from their job duties. Because work wasn't getting done, customer relations suffered. At another meeting, Sandy told her employees about a deal she was about to close with a new client. One excited employee told someone outside the company about the new client. This leak of information enabled a competitor to develop a stronger proposal and steal away the new client. Losing that deal forced Sandy to lay off employees, go deeper into debt, and finally dissolve the company.

Think Critically

1. How do you determine what company information should be reserved for management and withheld from employees?
2. Would you have fired the employee who leaked the information regarding the potential new client? Why or why not?



© PhotoDisc/Getty Images

Carefully consider what information to share with employees.



© Digital Vision/Getty Images

Why should a manager encourage employees to share their opinions and ideas?

Delegate Responsibility

Many entrepreneurs have difficulty delegating responsibility. To **delegate** is to let other people share workloads and responsibilities. Employees who are given more responsibility are better motivated and contribute more to the company. Delegating responsibility to them allows you to make the most of their experience, talents, and skills.

As a business owner, delegating allows you to focus on important items, such as expanding into new markets or offering new products. Assigning paperwork and other duties that can be performed by someone else will free up your time.

Finally, delegating responsibility is essential if a company is to grow. When your business is small, you may be able to handle all areas of its management. If the company is to expand, you will have to let managers take on more and more responsibility.

Listen to Employees

Some entrepreneurs fail to listen to their employees. In doing so, they miss out on an opportunity to take advantage of valuable ideas and resources that can help them increase profits.

The people who work for you are very familiar with your business and may be able to offer fresh ideas. Listening to new points of view may help you come up with new, creative solutions. If you value the opinions of your employees, they will feel they are a valuable asset to your company. This feeling of importance will keep them motivated to do a good job for you.

Checkpoint

How can you motivate employees?



Control Human Resources

The controlling function of management involves setting standards for the operation of a business and ensuring those standards are met. In the area of human resources, it is necessary to establish performance standards for employees and then evaluate employees periodically to be sure they are meeting the performance standards. This process can help you identify outstanding employees who should be promoted and problem employees who should be dismissed.

Evaluate Employees

Most businesses perform an employee review once or twice a year in which they analyze each employee's performance and determine the increase in the employee's salary. The job description should be used when evaluating how well an employee has fulfilled all of his or her job responsibilities. Some of the items that are usually evaluated include dependability, punctuality, attitude toward job and coworkers, and success in achieving predetermined objectives.

A **performance evaluation** serves as a management control tool that helps determine whether the objectives for a particular job are being met. The evaluation process is also useful to the employee. It helps the employee recognize strengths and see where there is room for improvement. As part of the process, plans for mentoring, training, and practice should be put in place to help improve the employee's performance in areas where needed.

During the performance review, the reviewer should focus on the positive aspects of the employee's performance. Productivity should be reviewed, and the employee and reviewer should work together to set new objectives for the upcoming period. The review should be recorded on an appraisal form. The form should include the employee's name and job title, as well as the manager's name, the date range the review covers, job responsibilities and attributes, places for comments, goals for the next year, and a section outlining plans for employee development. A ranking method can be used to easily mark how well the employee has performed.

Performance reviews should be conducted face to face. A written summary of the review should be kept in the employee's file.

Promote Employees

Promoting good employees will help ensure that they remain interested in working for your business. Employees often compete with one another, so promoting one over the other may cause problems. Be sure you make all decisions fairly. Base your decisions on solid reasons, such as volume of sales and quality of customer service.



© PhotoDisc/Getty Images

Why are performance evaluations important to both the employer and employee?

PERFORMANCE APPRAISAL

DATE: January 21, 20--

NAME: Daniel Tisdale

Reports To: Laureen Stiles

JOB TITLE: Marketing Director

Review Period: 1/1 to 12/31

ATTRIBUTE	WELL ABOVE STANDARD	ABOVE STANDARD	STANDARD	BELOW STANDARD	FAR BELOW STANDARD
Quantity of work		✓			
Knowledge of work		✓			
Ability to organize			✓		
Ability to meet deadlines			✓		
Dependability			✓		
Judgment			✓		
Initiative	✓				
Communication				✓	
Management of others			✓		
Teamwork			✓		

COMMENTS

You have done an outstanding job of increasing sales. Your hard work, dependability, and initiative are very much appreciated.

AREAS FOR IMPROVEMENT:

1. Increase technical knowledge to improve the quality and quantity of work.
2. Improve written communication skills by enrolling in a business writing course.
3. Improve management skills, in particular by delegating more responsibility to your marketing assistants.
4. Increase ability to participate as part of team.

GOALS FOR COMING YEAR:

1. Increase store sales 12 percent.
2. Oversee completion of company web site.
3. Generate online sales of \$75,000.

Employee: Daniel Tisdale

Manager: Laureen Stiles

Daniel TisdaleLaureen Stiles

Dismiss Employees

Some employees may not work out. In fact, they may end up hurting your business. How will you handle such situations? As soon as you notice an employee not performing well or causing problems, discuss the situation with him or her. If performance does not improve, issue a written warning. If there is still no improvement, you will need to dismiss that employee. Record the reasons for the dismissal.

Checkpoint

Why is it important to conduct employee performance evaluations at regular intervals?

11.3 Assessment

THINK ABOUT IT

1. What is the difference in a Theory X and a Theory Y manager? Which leadership style do you think is more effective? Why?
2. Why do many entrepreneurs find it difficult to delegate?
3. Why do you think it is important to keep a written summary of a performance evaluation?

MAKE ACADEMIC CONNECTIONS

4. **COMMUNICATION** Barry Sandler, owner of Sandler's Custom Computers, has decided to change the way sales associates are paid. Salaries are by commission only—hourly wages are not paid. Barry wants to get suggestions from his sales team. Your teacher will role play Barry Sandler. You and other students will role play the sales associates. As a class, decide on a new compensation method.
5. **COMMUNICATION** Using the Activity CD, open the activity "Performance Evaluation." Print a copy. With a partner, role play an employee and employer participating in a performance review. Assume the employee is a good worker who deserves a promotion. Make up the employer and job. Complete the performance evaluation form.



TEAMWORK

You manage a department in a business that is in the midst of change. Your employees have heard many rumors about job changes, possible layoffs, and pay reductions. Morale in the department is at an all-time low. Working with teammates, develop a plan to motivate your employees to achieve high performance standards and keep a good attitude in the midst of all the changes. Share your motivational plan with the rest of the class.



Sharpen Your Entrepreneurial Skills

Promoting Teamwork

In many activities, the ability to work together as a team determines whether or not a group's efforts will be successful. A sports team cannot win if its players do not work well together. Astronauts working on the space station cannot complete their mission if crew members do not cooperate.

Teamwork is important in many businesses. Employees who work as a team are usually very committed. They are more likely to work harder and to come up with creative ideas for increasing profits.

You will want your business to have an environment in which employees feel part of a team and work toward common goals. Respecting, communicating with, and getting along with coworkers are all important team behaviors. Creating this type of atmosphere can be a challenge.

As the owner of the business, it will be up to you to provide the leadership that will allow your employees to work together as a team. To be an effective team leader, you will need to do the following.

- Establish trust among team members and gain their trust.
- Make sure that all team members understand the goals you have set for the business.
- Encourage team members to be creative and innovative.
- Make team members feel like partners in your business.
- Help team members learn from their mistakes.
- Build the team's commitment to achieving the goals you have set.



© Digital Vision/Getty Images

TRY IT OUT

Effective teams not only need good leadership but also require committed team members. Working in teams, brainstorm a list of personal qualities that effective team members should possess. Provide examples of teamwork that you have observed and how the team used these qualities to achieve a common goal.

Chapter 11 | Assessment

SUMMARY

11.1 Identify Your Staffing Needs

1. To determine staffing needs, list all the duties in your business, identify how much time is needed to perform each one, determine the skills and qualifications employees need, and write job descriptions that list the specific responsibilities of each position. You should also create an organizational structure to show the relationships between the various jobs in the company.
2. To recruit new employees, you may use classified advertisements, online career and employment sites, employment agencies, college placement centers, in-store advertising, and referrals.
3. In addition to hiring permanent employees, you can also hire freelancers, interns, or temporary workers.

11.2 Staff Your Business

4. The four steps in the hiring process include (1) screen candidates, (2) review and verify job applications, (3) interview the best candidates, and (4) make a job offer.
5. A compensation package should include a method of pay and may provide a variety of benefits. Methods of pay include wages, salary, commission only, or a combination of salary plus commission. Bonuses and profit sharing are other compensation methods. Benefits may include paid leave for vacation and sickness; medical, dental, life, and accident insurance; and retirement plans.
6. Employers must follow all laws and regulations that are created to protect employees from unfair labor practices.

11.3 Direct and Control Human Resources

7. Implementing your staffing plan effectively requires that you have good management and leadership qualities. By enforcing policies and offering training, you will help your employees perform better.
8. There are several ways to motivate employees, including paying them well, treating them fairly, recognizing them for good work, and giving them adequate responsibility.
9. You should create a procedure for evaluating employees. Outstanding employees should be promoted when opportunities become available, and problem employees should be dismissed.

What do you know now?

Read *Ideas in Action* on page 299 again. Then answer the questions a second time. How have your responses changed?

VOCABULARY BUILDER

Match each statement with the term that best defines it. Some terms may not be used.

1. A written statement listing the tasks and responsibilities of a position
2. The process of determining the tasks and sequence of tasks necessary to perform a job
3. A management control tool that determines whether objectives for a job are being met
4. To look for people to hire and attract them to the business
5. People who provide specialty services to businesses on an hourly basis or by the job
6. Payments for labor or services that are made on an hourly, daily, or per-unit basis
7. An amount paid for a job position stated on an annual basis
8. A percentage of a sale paid to a salesperson
9. Financial reward for employment service in addition to salary
10. To let other people share workloads and responsibilities

- a. benefits
- b. bonus
- c. chain of command
- d. commission
- e. delegate
- f. freelancers
- g. interns
- h. job analysis
- i. job description
- j. performance evaluation
- k. profit sharing
- l. recruit
- m. salary
- n. staffing
- o. wages

REVIEW YOUR KNOWLEDGE

11. **True or False?** Good employees and a well-run human resource management program are as important to your business as are capital, equipment, and inventory.
12. A collection of tasks and responsibilities that an employee is responsible to conduct is a
 - a. job
 - b. job description
 - c. job analysis
 - d. duties and task list
13. Which of the following is *not* a way to motivate employees?
 - a. pay them well
 - b. treat them fairly
 - c. recognize them for good work
 - d. make all decisions for them
14. **True or False?** The job analysis helps people in a company understand who reports to whom.
15. Which of the following would *not* be included in a job offer?
 - a. job analysis
 - b. starting salary
 - c. terms of employment
 - d. benefits package
16. **True or False?** During the screening process, you determine which candidates are most qualified for the position you are trying to fill.
17. If you live in a very small community with a limited pool of available workers, what would be the *best* way to recruit employees from nearby communities?
 - a. online advertisement
 - b. in-store advertising
 - c. classified ad in the local paper
 - d. college placement center for a university 300 miles away

18. You interviewed a candidate for a sales position you have in your swimming pool sales and installation business. Sales are usually high in the spring and summer and then drop off in the fall and winter. The candidate has a family and needs a steady income but likes the idea of earning more pay if he makes a large number of sales. Which payment method do you think he would prefer?
 - a. wage
 - b. salary
 - c. commission only
 - d. combination plan
19. Offering an employee the opportunity to participate in your group health insurance plan is an example of a
 - a. wage
 - b. salary
 - c. bonus
 - d. benefit
20. **True or False?** The Occupational Safety and Health Act establishes the maximum number of hours employees can work.
21. **True or False?** The Family Medical Leave Act makes it possible for both men and women to take leave in the event of a birth or adoption of a child.
22. A ___?___ manager works directly with the workers on the job and is responsible for implementing the plans of middle management.
23. **True or False?** As long as a job candidate has the appropriate skills needed, it is not necessary to check his or her references.
24. Which of the following would be the most effective training method to use for an employee who needs to learn about the latest technology trends for today's modern office?
 - a. on-the-job training
 - b. coaching
 - c. mentoring
 - d. conference or seminar

APPLY WHAT YOU LEARNED

25. You have decided to hire three people to help in your custom drapery business: an administrative assistant, an interior designer/salesperson, and a sewer. What qualifications and skills must each of these employees possess? Write a job description for each position. Also, establish a compensation package for each position describing the type of pay and the benefits included.
26. For each of the positions you have established in your custom drapery business above, describe how you will recruit these employees. Create a want ad and prepare a list of interview questions for each position.

MAKE ACADEMIC CONNECTIONS

27. **MATH** Jayne Smith sells vacuum cleaners and is compensated under a combination plan. She earns \$9.25 per hour plus 15 percent of whatever she sells. Last month, Jayne worked 160 hours and sold 9 vacuum cleaners. Five of the vacuum cleaners were top-of-the-line models with a price of \$1,100 each. The remaining vacuum cleaners were \$450 each. What is Jayne's compensation for last month?

- 28. PROBLEM SOLVING** One of your employees is upset that another employee received a promotion. She thinks she should have gotten the job because she has been there longer and has always had good performance evaluations. What are some reasons that a newer employee would receive the promotion? How will you handle the situation?

WHAT WOULD YOU DO?



You want to hire a new sales assistant for your company. You checked with the local college placement office, and it sent several qualified applicants for an interview. You are really impressed with one of the candidates, and you want to hire him for the position. Before making the job offer, you decide to check the Internet to see if the candidate has a personal web page that might provide you with more information regarding his background and interests. By performing an Internet search, you quickly find his personal web page. You are shocked at some of the pictures he has posted and at some of the activities in which he has participated. What would you do? Would you hire him anyway or would this change your impression of him?

BUILD YOUR Business Plan *Project*

This activity will help you determine staffing needs for your business. This information will help you develop the Operations section of your business plan.

1. Assume your business will grow over the next year and you will need to add employees. Make a list of at least five jobs that need to be filled. Is each job a full-time job, part-time job, or temporary work? For each job, write a detailed job description. Create an organizational chart for your business based on these new positions.
2. Write a classified advertisement for each of the jobs you will need to fill. What employee characteristics and qualifications are you seeking? Write the interview questions that you will ask the candidates for each position. Write a list of questions you will ask their references.
3. For each position, create a complete compensation package that outlines wages or salary and any nonsalary benefits. Explain why you have structured the compensation package as such.
4. Add policies concerning vacation, holidays, hours, acceptable dress, and any other issues that affect your employees to the operating procedures manual you previously created in Chapter 10.
5. Create a sample performance appraisal form for your employees. Will you use the same form for each position? Why or why not?
6. Determine the ways you plan to motivate your employees. Create at least one method of publicly acknowledging employees for good work. Record your ideas.
7. In what ways will you train new and existing employees for your business? What aspects of your business require training, and what type of training is the best for each aspect? Write a short report about your decisions.

Planning a Career in Audio-Video Technology



"My aunt got married last weekend and the wedding was a blast. Both a photographer and a videographer were at the wedding. During the reception, the photographer set up a laptop on a table that had photos of the ceremony streaming on screen. It was really fun to see pictures of the ceremony while we were still celebrating the wedding."

How do people determine the best way to record significant events in their lives? How do companies develop portfolios of their products for use in printed catalogs or on web sites?

Photographers take pictures of people, events, and products. Photographers often specialize by topic. Areas of specialization include news, commercial, fine arts, portrait, or special event photography.

EMPLOYMENT OUTLOOK

- Average growth is anticipated.
- Competition for positions is fierce as many people find this field appealing.
- Individuals who keep current with technological changes in equipment and processing will have the most opportunities.

JOB TITLES

- News Photographer
- Children's Photographer
- Soft Goods Photographer
- Online Photographer
- Event Photographer
- Portrait Photographer

NEEDED SKILLS

- Creativity and a solid understanding of the photographic process are essential.

- Strong interpersonal skills are required—especially for portrait photographers who work with a diverse client base.
- Independent photographers should be Internet savvy to facilitate direct marketing to clients.
- Strong computer skills are needed for digital photo manipulation.

What's it like to work in Audio-Video Technology

On Sunday afternoon, Keisha, a self-employed freelance photographer, went to a local park to take a combination of candid and posed pictures for a family reunion. Sunday evening Keisha loaded the family reunion photos on her web site. Although Keisha charged a fee for taking photos at the reunion, she was able to generate additional revenue when family members purchased either individual photos or customized albums.

Monday morning Keisha met with a newly engaged couple who were potential clients. After discussing the logistical details of the wedding, Keisha showed the couple a few albums from prior weddings. She then walked the couple through her web site. By providing digital copies of the photos online, categorized by various stages of the wedding, it was easy for couples to review photos. Album viewers could simply click a tab like "Ceremony" or "Reception" to view the photos of most interest.

What about you? Would you like to help a variety of individuals record special events through the use of photography?



BUSINESS PLAN

Business plans are an effective tool for evaluating, organizing, and selling a new business concept. A well-developed business plan can be a key component for a successful business startup. Participants must demonstrate an understanding and mastery of the process required in developing and implementing a new business venture. The project may be completed by teams of two to three members. The business plan must include the following sections: Executive Summary, Company Description, Industry Analysis, Target Market, Competitive Analysis, Marketing Plan and Sales Strategy, Operations, Management and Organization, Long-Term Development, and Financials. Many business plans also include copies of key supporting documents, such as certifications, licenses, tax requirements, and codes, in an appendix.

Proposals may describe a proposed business venture or a current business operation. The business idea must be currently viable and realistic. The *Build Your Business Plan Project* that you have been working on could be used in this competitive event. Teams have seven minutes to present their business plan and to describe the project and results obtained. Visual aids and samples specifically related to the project may be used in the presentation. Judges have three minutes to ask questions following the presentation.

PERFORMANCE INDICATORS EVALUATED

- Design and conduct a marketing research study.
- Prepare a written proposal for a new business based on the research.
- Request financing for the proposal from a venture capitalist.
- Demonstrate effective communication skills.
- Derive facts from data, findings from facts, conclusions from findings, and recommendations from conclusions.
- Demonstrate critical thinking/problem-solving skills.
- Prioritize time and meet deadlines.
- Identify the target market and the competition within the market area.
- Demonstrate the ability to be an effective team participant.
- Develop a concept from an idea to an actual proposal.

Go to the FBLA web site for more detailed information.

Think Critically

1. Why must the business proposal cover possible risks?
2. What target market demographics are important to research?
3. Why must the team present a strong work ethic?
4. Why should the team conduct marketing research before making the presentation?

www.fbla.org

Chapter 12

© Digital Vision/Getty Images



Risk Management

12.1 Business Risks

12.2 Insure Against Risks

12.3 Other Risks

school.cengage.com/entrepreneur/ideas

IDEAS IN ACTION

Growth Is Risky

Scott Alterman earned money at an early age by starting several small businesses in high school. After college, Scott joined his brother, Greg, who was running Gagwear, a small company in Atlanta that served the corporate market with customized apparel.

The Alterman brothers began manufacturing edgier and higher-quality apparel than what was typically offered in their target market. They started with caps that included their own label with a phone number on them. They took a risk by importing thousands of caps before they had sold one. Their customers took notice. Ironically, they had many inquiries from competitors wanting to buy the blank hats, so they decided to start a “blanks” division. This was the beginning of Alternative Apparel, the wholesale division. Scott concentrated his efforts on Gagwear, while Greg developed Alternative Apparel.

Gagwear’s customer base was small to medium-sized corporate customers. Scott wanted to grow Gagwear by calling on retailers and larger customers. So another company, The Icebox, a full-service advertising-specialty company serving small to medium-sized companies, was born. The Alterman brothers brought in a partner, Jordy Gamson, to run The Icebox. Later, Scott and Jordy decided to merge Gagwear and The Icebox divisions and operate both under The Icebox name. Greg is now running Alternative Apparel while Scott and Jordy run The Icebox.

Meanwhile, Alternative Apparel had begun to experience serious growth. The decision was made to completely separate Alternative Apparel and The Icebox to let them grow properly. The businesses quit sharing employees, and each got financing to evolve on their own.

The growth of The Icebox did not come without risks. With a \$2 million note for his new building along with a \$1.2 million line of credit, Scott faces financial risk. He also faces risks by extending credit to customers. Because he wants to be customer-friendly, Scott sometimes extends credit to customers other businesses would consider too risky. On the other hand, now that The Icebox is a separate company, Scott has eliminated some of the risks associated with the production side of his business. Rather than incur the financial risks of buying and repairing equipment and hiring production employees, The Icebox uses contract companies for screenprinting and embroidery.



© Scott Alterman

What do you know?

1. What unmet need did the Alterman brothers uncover?
2. How is Scott taking a risk by extending credit to customers?
3. Why is contracted work less risky for The Icebox?

12.1 Business Risks

Goals

- List and explain steps involved in preparing to face risks.
- Discuss types of theft and security precautions that can be taken to protect your business.

Terms

- risk
- risk management
- risk assessment
- shoplifting
- bounced check

Focus on Small Business

What if disaster strikes?

"Kristin," Ty asked his partner, "what do you think would happen to our web hosting business if our computers or computer data were stolen or hacked into?"

"Wow, Ty, we've never really thought about that. We just come in every day and do our work. We do back up our work periodically, but we just put the CDs in our file cabinet."

"I know," Ty responded, "I started thinking about it after I read about a business that had all of its computers stolen one night. And I realized we have no emergency plan in place."

"We sure don't, but I bet we will have something figured out by tomorrow!" Kristin said.

Work as a Team What risks do you think Ty and Kristin would face if all their computers were destroyed or computer data were compromised? What steps do you think they should take to be prepared in case this should happen?



© PhotoDisc/Getty Images

Businesses must address computer security risks.

Dealing with Business Risks

As an independent businessperson, you will face many risks. **Risk** is the possibility of some kind of loss. Risks can be categorized as human risk, natural risk, and economic risk. **Risk management** is taking action to prevent or reduce the possibility of loss to your business. You can avoid risk, assume risk, or transfer risk.

Identifying Risks

Human risks are those caused by the actions of individuals, such as employees or customers. Examples include shoplifting, employee theft, robbery, credit card fraud, and bounced checks. *Natural risks* are caused by acts of nature. Examples are storms, fires, floods, and earthquakes. The occurrence of any of these could bring about tremendous loss to a business. *Economic risks* occur because of changes in business conditions.

Preparing to Face Risks

As an entrepreneur, you must be prepared to face all kinds of risks. You will need to decide the best strategy for dealing with risks. You may decide to avoid the risk. For example, if you think a product you are developing will not meet market needs, you may decide to avoid financial risks caused by low sales by halting production of the product.

You may decide to assume the risk if you determine the risk is low. If your market research indicates the product you are developing will be successful with your target market, you will most likely produce and sell the product even though there is still a chance of lower sales than expected.

Transferring the risk is another option. You will be able to protect yourself against the financial losses from some risks by purchasing insurance. Insurance transfers the risk of financial loss to the insurance company.

You never know when a loss may occur, but you should have a plan of action in place when it does. When Hurricane Katrina struck New Orleans in 2005, many business owners were not prepared for the loss of property and income that occurred. You need a plan in place so that if something does happen, you can recover and restart business operations quickly. To prepare for risks, you should do the following:

1. Determine what can go wrong.
2. Develop a plan.
3. Communicate your plan.

DETERMINE WHAT CAN GO WRONG As a business owner, the first thing you need to do is conduct a risk assessment. A **risk assessment** involves looking at all aspects of your business and determining the risks you face. During this assessment, you should:

- Learn the risks your business faces.
- Decide how the risks would affect your business.
- Prioritize the risks by the impact they will have on your business.

DEVELOP A PLAN Once you have identified the risks that could affect your business, you should develop a written plan for dealing with them. When developing a risk management plan, you may have to comply with certain laws. For example, OSHA (Occupational Safety and Health Administration) requires businesses to have an evacuation plan for emergencies. There are many good sources available to help you establish an effective risk management plan. If you are developing an emergency action plan, the National Safety Council, a nongovernmental organization that promotes safety, is a good source. It recommends that the following items be included in your emergency action plan.

- Chain of command information including names and job titles of the people responsible for making decisions, monitoring response actions, and recovering back-to-normal operations
- The names of individuals responsible for assessing the degree of risk to life and property and who should be notified for different types of emergencies

★ Develop Your Reading Skills

As you read, use the SQ3R method:

- Survey the chapter to get an idea of what you will be reading.
- Make a list of Questions about the chapter that come to mind as you survey.
- Read the chapter.
- Recall what you have read.
- Review the material by discussing it with a classmate.





© PhotoDisc/Getty Images

Why is it important to have a plan for handling risks?

- Preferred method for reporting fires and other emergencies
- Specific instructions for shutting down equipment and other business activities and procedures for employees who must shut down equipment before they evacuate the facility
- Facility evacuation procedures including maps showing the best and alternate exit routes
- Specific training for those responsible for responding to emergencies

Be sure to have a recovery plan in place if you suffer a setback. A *recovery plan* will enable you to get back to business as quickly as possible. If you suffer a loss due to a fire, have a plan for temporarily relocating, getting replacement equipment, and retrieving lost data. If one of your suppliers is out of stock of a component needed in the production of your product, have another supplier lined up. A recovery plan will help you continue to meet your customers' needs.

COMMUNICATE YOUR PLAN Let your managers and employees know about your plan for handling risks. To ensure your plan is carried out properly, assign activities and responsibilities to the appropriate people. For example, to protect against the risk of a faulty product, assign the production manager the task of checking the quality of the finished product. If you plan to run an advertisement for an upcoming sale, make sure someone is responsible for placing the ad in the appropriate media at the appropriate time to avoid the risk of lost sales. If you want to protect your computer system from the risks of viruses and computer hackers, you can work with a computer security expert. To address the risks related to emergencies, provide training for all employees to show them what to do in the event of any type of emergency. Work with your managers and employees to be sure all risks are addressed.

Checkpoint

What should you do to prepare for business risks?

Types of Theft

One of the biggest risks that businesses face is theft. Shoplifters and employees may steal your merchandise. Burglars may break into your business and steal your equipment. Customers may use stolen credit cards or write checks when they don't have money in their account. Once you have identified the theft risks you face, you can determine what security precautions you need to take.

Shoplifting

Shoplifting is the act of knowingly taking items from a business without paying. Customers shoplift millions of dollars in merchandise every year. The problem exists in virtually every type of retail business.

If you own a retail business, you will have to take steps to prevent or reduce shoplifting. Some of the things you can do include the following:

1. Instruct your employees to watch for customers who appear suspicious.
2. Hire security guards or off-duty police officers to patrol your store.
3. Post signs indicating that you prosecute shoplifters.
4. Ask incoming customers to leave their bags behind the counter.
5. Install electronic devices, such as mounted video cameras, electronic merchandise tags, and point-of-exit sensors, to detect shoplifters.

Employee Theft

Most employees are hard working and honest, but there are a few who will take things from your business, such as office supplies, equipment, merchandise, and even money. These employees can negatively impact your business financially.

As an entrepreneur, you need to be aware of the possibility of employee theft. You need to take steps to prevent the problem from occurring. You also need to know how to detect the problem and to handle it once it is detected.

Some businesses, such as restaurants and retail stores, are more vulnerable to employee theft than others. If you own such a business, you may need to adopt the following procedures:

1. **Prevent dishonest employees from joining your company.** Screen job applicants very carefully. Consider using a company that specializes in verifying job applicants'

NETBookmark

More than 135,000 convenience stores operate in the United States. About 6 percent of all U.S. robberies occur at convenience stores. The Association for Convenience and Petroleum Retailing is a trade association for convenience store operators. The group has created some robbery awareness/deterrence tips for members to use in their stores.

Access school.cengage.com/entrepreneur/ideas and click on the link for Chapter 12 to learn more about these tips. Which of the tips do you think would be most effective in deterring robbers? Explain. Why do you think greeting and paying attention to every customer who enters the store is an effective deterrent to crime? Do you think stores that stay open 24 hours a day are at greater risk for robbery? Why or why not?

school.cengage.com/entrepreneur/ideas

educational backgrounds and searching their criminal records, driver's license reports, civil court records, and credit reports.

2. **Install surveillance systems.** Often the mere knowledge that they are being monitored by a video camera deters employees from stealing.
3. **Establish a tough company policy regarding employee theft.** Your company policy should detail the consequences of employee theft. Make sure that all employees are aware of the policy.
4. **Be on the lookout.** Watch for cash discrepancies, missing merchandise or supplies, vehicles parked close to loading areas, and other signs that something may be wrong. Keep an eye on employees who seem to work at odd hours, perform their jobs poorly, or complain unreasonably. Make inquiries if an employee has an unexplained close relationship with a supplier or customer or has a personal lifestyle that seems inconsistent with his or her salary.



© PhotoDisc/Getty Images

How can a business owner prevent shoplifting?

Robbery

Almost all businesses are vulnerable to robberies. You can choose what is considered a safe area of town to locate your business to guard against being robbed. You can also install dead-bolt locks and burglar alarms. To limit losses in the event of a robbery, many businesses keep a minimum amount of cash in the cash register. Once more than a certain amount is received, the cash is transferred to a safe. Some businesses also use surveillance cameras, which deter prospective robbers from entering the business in the first place. Be aware that you may be robbed regardless of the number of preventative measures you take. It is simply a risk of being open for business.

BE YOUR OWN BOSS

You are the owner and manager of a diner located along a busy interstate highway. You do a good business with travelers passing through as well as locals who eat with you regularly. Recently, there have been several robberies during operating hours in nearby businesses. Your local customers are beginning to get a little nervous about coming to your business. Outline a plan to minimize your risk of robbery. Include ways to make your customers feel safe.

Credit Card Fraud

Business owners lose millions of dollars every year because of stolen credit cards. If a purchase is made on a stolen credit card, a business may not be able to collect the money. To prevent stolen credit cards from being used to purchase goods, you can install an electronic credit authorizer. This machine checks to see if a credit card is valid. If the card has been reported stolen or if the cardholder has exceeded the credit limit, authorization will not be granted.

Bounced Checks

A **bounced check** is a check that is returned to you by the bank because the customer's checking account has insufficient funds to cover the check amount. Bounced checks are also called *bad checks*. Preventing losses from bad checks is difficult. To minimize losses, you can establish a policy of accepting checks drawn on in-state banks only. You can also charge a fee if a customer writes a bad check to your business. Asking for identification, such as a driver's license, can help you track down a person who writes you a bad check so that you can collect the money due. If bad checks are a serious problem in your area, you may decide not to accept checks at all.

Checkpoint

How can you protect your business from theft?

12.1 Assessment

THINK ABOUT IT

1. What are the categories of business risk? Provide three examples of each.
2. What are some steps that you can take to minimize employee theft?
3. You own a pizza shop. You suspect that one of your delivery people is charging customers more than what they actually owe and keeping the difference. How would you handle this situation?

MAKE ACADEMIC CONNECTIONS

4. **MATH** At closing, the Old World Café's cash register receipts totaled \$884. The cash in the register equaled \$534, and the credit card slips equaled \$237. How much of the proceeds are not accounted for? What might explain the difference?
5. **COMMUNICATION** Think about your school as if it were a business. How can your school identify and deal with the risks it faces? Using the Activity CD, open the activity "Risk Management Plan." Print a copy and complete the activity. Share your plan with the class.



TEAMWORK

Last year, the holiday season profits at Ray's Sporting Goods were reduced significantly because of shoplifting. Form teams and brainstorm ways to approach the problem this year. Put together a proposal containing your recommendations for Ray. Share your recommendations with the rest of the class.





12.2 Insure Against Risks

Goals	Terms
<ul style="list-style-type: none"> • Classify risks faced by business owners. • Explain why some business risks are uninsurable. • Determine the different types of insurance you need for your business. • Explain how to approach an insurance purchase. 	<ul style="list-style-type: none"> • premium • pure risk • speculative risk • controllable risk • uncontrollable risk • insurable risk

Focus on Small Business

A river runs through it

Carlos thought he had found the perfect location for his new restaurant. He wanted to have a large outdoor patio with a great view, and this location had exactly what he wanted. The patio looked out over a river, and there were many beautiful shade trees. Carlos decided to talk to the former owner of the previous restaurant that had occupied the site. He told Carlos that the restaurant had flourished until the river flooded and caused extensive water damage. The previous owner made the repairs but was never able to recover financially, so he went out of business. This concerned Carlos and made him wonder if this was really the ideal spot.

Work as a Team What do you think Carlos should do? If he decides to locate here, what can he do to protect his investment?



Without taking precautions, some businesses may be forced to close.

© PhotoDisc/Getty Images

Classification of Risk

As a business owner, you are at risk from more than just criminal activity. A fire could destroy your building. An accident could injure an employee. A broken water pipe could ruin your inventory. A precaution you can take to protect against financial loss is to purchase insurance. A payment made to an insurance company to cover the cost of insurance is a **premium**. It is the price paid to cover a specified risk for a specific period of time.

Business owners face many types of risk. The classifications of risk are based on the result of the risk, controllability of the risk, and insurability of the risk.

Result of the Risk

A **pure risk** presents the chance of loss but no opportunity for gain. If you have a vehicle that is used in your business, every time it goes



© PhotoDisc/Getty Images

What are some ways that a jewelry store could control the risks it faces?

did you KNOW?

According to the Insurance Information Institute, Hurricane Katrina was the most costly catastrophe in the United States with over \$42 million of loss.

out on the road there is the risk of an accident. If there is an accident, loss will likely be suffered. However, if an accident is avoided, there is no opportunity for gain.

A **speculative risk** offers you the chance to gain as well as lose from the event or activity. Investing in the stock market is a good example of a speculative risk. When you invest money, you have the chance to make money if the stock price rises. However, if the stock price falls, you risk the chance of losing money.

Controllability of the Risk

A **controllable risk** is one that can be reduced or possibly even avoided by actions you take. Installing a security system in your business could lessen the risk of your business being robbed.

An **uncontrollable risk** is one on which actions have no effect. The weather cannot be controlled, but it can have a tremendous effect on some businesses. If a hurricane hits a resort town, a dramatic decrease in business and loss of profit will result. But if the weather is sunny and warm, tourism will flourish and business owners may make a profit.

Insurability of the Risk

A risk is an **insurable risk** if it is a pure risk faced by a large number of people and the amount of the loss can be predicted. Buildings that house businesses are susceptible to fire. Nearly all businesses face this risk, and past statistics can help insurance companies predict the amount of loss and percentage of businesses that will suffer fire losses annually. Insurance companies can sell fire insurance to help cover losses. The premiums of all those insured are pooled and used to help those who incur losses.

If there is a risk that a loss will occur and the amount of the loss cannot be predicted, the risk is *uninsurable*. An insurance company would have no way of determining the premiums to charge or the amount of funds to pool to cover unpredictable losses. A business may



move to a new location, and customers may not follow. The loss of income that could result cannot be predicted and, thus, is not insurable.

Checkpoint

What is the difference between a pure risk and a speculative risk?

Uninsurable Risks

Sometimes things happen in the business world that are not covered by insurance, which can be very costly to a business. Insurance does not cover risks that cannot be reasonably predicted or for which the financial loss to the business cannot be calculated. These risks are tied to economic conditions, consumer demand, competitors' actions, technology changes, local factors, and business operations.

Economic Conditions

Managers must constantly study economic conditions. Changes in economic conditions can result from an increase or decrease in competition, shifts in population, inflation or recession, and government regulations. World events can also result in economic changes. The events of September 11, 2001, caused a dramatic downturn in the U.S. economy, resulting in major cutbacks and layoffs by businesses. This decreased the amount of disposable income for many Americans, which resulted in many entrepreneurs losing their businesses. When the economy takes a downward turn, a business must respond quickly by cutting production and expenses.

Consumer Demand

Businesses produce products and services that they think consumers want to buy. Before going into business, business owners must research consumer needs and wants. If they can predict a change in demand, they may be able to profit by producing and selling a new product or service. However, if consumer demands change suddenly, the company may end up with products in their inventory that they cannot sell for a profit.

Competitors' Actions

Business is competitive. As a business owner, you must be aware of your competitors and their actions. A major advertising campaign or a drop in price by your competitors may result in a change in your volume of sales. You must be ready to respond to actions by your competitors to minimize the risk to your business.



© Digital Vision/Getty Images

How might the actions of one computer manufacturer pose a risk to another computer manufacturer?

Technology Changes

Changes in technology bring about changes in business. As a business owner, you need to stay up to date on technology trends. Evaluate new technology and see if it can help your business. Updates to technology can be a major expense but can alternatively provide efficiencies and help you serve customers better. If customers view your business as outdated, you may lose customer loyalty and sales to your competition.

Local Factors

Businesses can suffer due to activities that occur in their local community. If there is an increase in local taxes or a change in local business regulations, it can affect your business. If a local government makes an improvement to the infrastructure, such as a road or utility improvement, it can help your business in the long term. In the short term, it may result in a loss of business because ongoing construction could cause customers to detour around your business.

Business Operations

The management of a business contributes directly to the success or failure of the business. A business that is poorly managed can have high employee turnover, poor customer service, higher expenses, and other problems. Poorly trained employees can also cause operational problems. Managers and employees must work together to ensure the success of the business.

Checkpoint

Why are some risks uninsurable?

Types of Insurance

Purchasing insurance is one of the best ways you can prepare for the unexpected. There are many options for insurance. You will have to examine the risks you identify and their potential impact on your business to determine if you need to insure against the risk.

Business Insurance

Insurance companies selling business insurance offer policies that combine protection against all major property and liability risks in one package. These coverages are also sold separately. Package policies are created for businesses that generally face the same kind and degree of risk. Large companies might purchase a commercial package policy or customize their policies to meet the special risks they face. Many small and mid-sized businesses purchase a package known as a business owner's policy (BOP). Business owner's policies typically include the following:

- **Property insurance** This type of insurance provides coverage for damage to buildings and the contents inside the buildings, such as furniture, fixtures, equipment, and merchandise owned by the business.



- **Business interruption insurance** This type of insurance covers the loss of income resulting from a fire or other catastrophe that disrupts the operation of the business. It can also cover the extra expense of operating out of a temporary location.
- **Liability protection** This type of insurance covers your company's legal responsibility for the harm it may cause to others as a result of what you and your employees do or fail to do in your business operations. Harm may involve bodily injury or property damage due to defective products, faulty installations, and errors in services provided.

BOP's do not cover auto insurance, workers' compensation, or health and disability insurance. They also do not cover professional liability, which involves claims of negligent actions by business professionals such as doctors. You will need separate insurance policies to cover these items.

Life Insurance

Life insurance is paid in the event of the death of the insured. It is intended to provide financial support for families should the income earner die. A business owner may buy life insurance so that his or her heirs have enough money to continue the business.

Other Kinds of Insurance

Other types of insurance that you may want to purchase include flood, crime, and renter's insurance. Flood protection is not standard with property insurance, so you may have to purchase it separately. Crime

WHAT WENT WRONG ?

Goodbye, Gorgeous!

Eddie opened her beauty salon "Hello, Gorgeous!" by taking out a \$40,000 loan to help pay for the renovations and equipment she needed to purchase. She had two hair stylists working in the salon as contract employees. They paid her monthly rent to use space in the salon. The combined rent they were paying helped cover about 50 percent of the monthly operating expenses.

Eddie took out a business owner's insurance policy for \$20,000 worth of coverage. Eddie was making enough money to pay her monthly expenses, but not enough to save at this point. After six months of being in business, there was a fire in the salon. Hello, Gorgeous! was completely destroyed. The cause of the fire was a curling iron that Eddie left on over the weekend.

Eddie still owed over \$35,000 on the business loan she obtained. Her contracted employees

immediately moved to another salon. Suddenly, Eddie was all alone without any income or savings and not enough insurance to cover her loan. She was forced to close Hello, Gorgeous! and take a job working at another salon to pay off her debt.

Think Critically

1. Do you think Eddie was prepared to deal with business risks?
2. What mistake did Eddie make when purchasing insurance?



Don't trim costs by buying less insurance coverage than you need.

© PhotoDisc/Getty Images

insurance protects against losses resulting from crime, such as robbery, computer fraud, or employee theft. Renter's insurance covers the contents owned by the renter inside the leased space. The actual owner of the building would purchase insurance for the building. Depending on your business and its location, you may or may not decide to purchase these additional kinds of protection.

Checkpoint

What types of insurance can you purchase for your business?

Buy Insurance

Buying insurance can be complicated. Is it possible to have too much or too little insurance? A good insurance agent can help you make decisions about insurance coverage.

Choose an Insurance Agent

Insurance is sold by agents. An agent can be independent and represent many different insurance companies or work for a single insurance company. Before selecting an insurance provider, talk to an agent who represents more than one insurer or ask representatives of several different companies to talk with you about their policies.

The market for insurance is competitive, so many agents will be eager to sell you insurance. To get the best price, contact a few agents and compare prices and policies. Then consider how you feel about the agents. Remember that the person who sells you the policy will be involved in processing your claim should you ever need to collect on your policy. It is therefore important to choose someone whom you trust. You may already have an agent you trust with your car insurance or other types of insurance. That agent can be a good starting point in your research.



Why is it important to “shop around” for an insurance agent?

Determine How Much Coverage You Need

To determine the kinds and amounts of coverage you need, start by making a list of the property you own. Include equipment, inventory, vehicles, and other significant assets, and put a value next to each. Then think about the kinds of risk you would like to insure against. If, for example, your business is located near a river that could flood, you may want to purchase flood insurance. If you live in a low-crime area, you may decide against purchasing insurance that covers break-ins. Understand, however, the implications of not having insurance if something should happen.

The next step is determining how much coverage you need. Be sure you have enough insurance to cover any and all debts you may have incurred while starting your business. Li-Li Tang, owner of Computer Systems, has a \$50,000 bank loan on her business, as well as two small



loans for \$5,000 each. She wants to get at least \$60,000 worth of property insurance to cover these outstanding debts in the event of a problem.

Insurance agents earn commissions on the amount of coverage they sell. To make sure you need all the coverage your agent suggests, talk to other business owners in your area or counselors from SCORE or the SBA.

Checkpoint

How can you determine how much insurance you need?

12.2 Assessment

THINK ABOUT IT

1. What factors determine the classifications of risk?
2. Provide three examples of risks that are uninsurable?
3. Tim Stanton has just opened a surf shop on the beach in South Florida. He has purchased property insurance to cover possible losses against his building, fixtures, equipment, merchandise, and other assets. Against what additional risks should he consider insuring his business?
4. What factors should you consider when choosing an insurance agent?

MAKE ACADEMIC CONNECTIONS

5. **MATH** You have taken out a loan for \$50,000 to start your business. As a condition of the loan, your bank requires you to carry property insurance for at least the amount of the loan. Your property is valued at a total of \$100,000. Your agent recommends you carry property insurance covering at least 80 percent of your property's value. If annual insurance premiums are \$15 per \$1,000 of coverage, how much will you pay for insurance to satisfy your bank loan requirement? How much will you pay if you follow your agent's recommendation?
6. **COMMUNICATION** You have just opened an insurance agency that specializes in insuring businesses. Write a sales letter to prospective customers introducing yourself and your services.



TEAMWORK

Choose a partner. One partner should assume the role of an entrepreneur who just took out a loan to open a roller skating rink. The other should play the role of an insurance agent who must educate the new owner about the types of insurance available. Working together, use the Internet and other resources to research information about the types of insurance a skating rink should carry. Then role play the conversation between the insurance agent and the business owner.

12.3 Other Risks

Goals

- Identify risks associated with credit.
- Explain how to manage risks at work.
- Describe strategies to reduce the risks of doing business internationally.

Terms

- trade credit
- consumer credit
- Federal Employees' Compensation Act (FECA)

Focus on Small Business

Risks are everywhere!

Dale realized that there were many risks he would face as a business owner. He wanted to learn as much as he could about risks before he opened his new sporting goods business. So, he called his friend Monica for some advice. Monica had been in business for almost two years and had gained valuable business experience.

"Dale, it's good that you came to me," Monica replied. "I've got lots of information for you. I know you have learned about insurable and uninsurable risks, but there are some hidden risks you might not think about. I thought I could increase sales and provide customers a convenient service by offering them a store credit account, but you wouldn't believe how many people never paid the first bill! Then, my maintenance employee fell off of a ladder while painting. He had to spend two weeks in the hospital. I could go on and on."

"Yes, Monica, I think you have given me plenty to think about. There are many more risks to consider than I was aware of!" Dale replied.

Work as a Team What do you think Dale can learn from Monica's experiences? What should Dale do to minimize the risks Monica mentioned?



© PhotoDisc/Getty Images

Beware of hidden risks.

Risks of Credit

As a business begins operation, there will be costs that will be too expensive for the entrepreneur to pay all at once. Credit makes it possible for the entrepreneur to make these costly purchases. The business owner will also have to make decisions about extending credit to customers. Extending credit can help increase sales. However, a business will need to decide if extending credit will result in an overall increase in income. Although credit is useful to a business when buying or selling, there are risks involved. It is important for you as an entrepreneur to understand these risks.



Why would a business offer a credit card if it risks not getting paid?

Types of Credit

Credit can be categorized according to whom the credit is offered. Like bank loans, the credit a business offers its customers can be secured or unsecured.

TRADE CREDIT When one business allows another business to buy now and pay later, it is offering **trade credit**. Many purchases a business owner will make from other businesses will be made with trade credit. The negotiated price of products purchased on trade credit will often be higher than the cash price. This is necessary because there is a lapse of time that occurs from when the sale is negotiated to when the products are actually delivered. Because of this delay in receiving payment, the supplier charges a higher price. As the business owner, you will need to be sure that you have the money to cover your expenses when they are due in order to protect your credit record.

On March 29, Raul Gomez places an order with Bear Creek Embroidery for three-dozen golf shirts with his company logo embroidered on them. On April 1, Bear Creek Embroidery negotiates the purchase of three-dozen shirts from Alternative Apparel on credit. The shirts are delivered to Bear Creek on April 15. Two weeks later, Bear Creek ships the shirts with the logos to Raul. It takes one week for the shirts to arrive and one week for Raul to process and pay Bear Creek's invoice.

The trade credit that Alternative Apparel extends to Bear Creek allows 60 days for payment. This enables Bear Creek to receive the shirts, add the logo, ship the shirts, and receive payment from Raul in time to send payment to Alternative Apparel.

CONSUMER CREDIT When a retail business allows its customers to buy merchandise now and pay for it later, it is offering **consumer credit**. Consumer credit is offered in two basic forms: loans and credit cards. A loan gives the individual a lump sum of money to spend and pay back

over time with interest. If a loan is secured, it is backed by something of value that can be taken and sold if the loan is not repaid. One type of secured loan offered by retail establishments is an *installment loan* that is paid back with interest in monthly equal amounts over a specified period of time. Many cars and home appliances are financed with installment loans with the financed item serving as the collateral.

An unsecured loan is granted based on the credit history of the individual. This type of loan is not backed by collateral. Most credit cards are considered unsecured loans. When a business offers its own credit card to customers, it will not receive payment for a month or more after the sale is made. Therefore, the business will need to make other arrangements to ensure it has money to cover expenses associated with the sale of the merchandise. If the customer does not pay, then the business owner can attempt to collect the money or take back the goods that were purchased.

Collection difficulties are one reason a business chooses to accept credit cards that are issued by banks or credit card companies, such as Visa, Discover, or MasterCard. The credit card company will pay the business for the amount of the purchase. The business is charged a fee by the credit card company that is a percentage of total credit sales. The credit card company is then responsible for collecting the amount charged from the customer.

If Raul Gomez offers a credit card to his customers, then Raul is responsible for collecting payment from the customer. However, if the customer pays with a Discover card, Mark gets his money from Discover, and Discover bears the burden of collecting payment from the customer.

Credit Policies

Once an entrepreneur decides to offer credit, policies must be established to help reduce risks. Policies should specify to whom credit will be extended, what products may be purchased on credit, and what the terms of the credit will be. The terms include the amount of credit, the rate of interest charged, and the length of time before payment is required.

It will be very important for the entrepreneur to determine what type of customer will be approved for credit. Most businesses offering credit cards have customers complete a credit application to determine whether they are *creditworthy*, or able to pay. If credit is extended to individuals who are not able to pay, the business loses all the money invested in the product. If the product is recovered, money will still be lost because used merchandise cannot be resold at the original selling price. Some things to consider in determining who is creditworthy include the following:

- Previous credit history
- Employment record
- Assets owned
- Money available for making payments (checking and savings accounts)
- Financial references



Collection procedures must be established and followed carefully. This will ensure that customers are billed on time. Procedures should state how to handle customers who do not pay on time or do not pay at all.

UNCOLLECTIBLE ACCOUNTS Businesses and credit card companies usually charge the customer interest on the balance due to cover the cost of the credit service. When accounts are paid on time, the interest is income for the business. However, even though a business is careful about deciding which customers are creditworthy, there is still the risk that some customers will not pay their account balances. These uncollectible accounts are an expense to the business and decrease net income.

Checkpoint

How can a business owner reduce the risks of offering credit?

Risks in the Workplace

Different occupations have different risks associated with them. Due to the nature of the work that is performed, some workplaces are considered to be dangerous. Some of the most dangerous occupations in America include timber cutters and loggers, commercial pilots, construction and iron workers, refuse collectors, farmers and ranchers, roofers, electrical power line installers, and cab drivers. Other occupations, although not classified as dangerous, do have risks associated with them. Individuals who work in hospitals can be exposed to viruses and bacteria that can cause disease or infection. Night clerks can be a target for a robbery. Even using a computer for long stretches of time can cause injury. *Repetitive stress injuries* result from performing the same activity repeatedly for long periods of time. They can be very painful and cause disabling injuries. With some exceptions, any harm suffered by employees at the workplace is considered to be a work-related injury.

Federal Employees' Compensation Act

The **Federal Employees' Compensation Act (FECA)** is a law that provides benefits to employees who have suffered work-related injuries or occupational diseases. These benefits include payment of medical expenses and compensation for lost wages. The FECA also provides for payment of benefits to dependents of employees who die from work-related injuries or diseases.

Employers are required by law to carry insurance to protect against these risks. This insurance is called workers' compensation. The



© PhotoDisc/Getty Images

Why are employers responsible for carrying insurance on their employees?

expense for this insurance is entirely the employer's responsibility. No part of this insurance expense is paid by an employee.

Workers' Compensation

Workers' compensation laws vary from state to state but generally provide for the payment of medical bills, a percentage of lost wages, and vocational retraining if an employee is unable to resume his or her former job. Workers' compensation will also pay a death benefit to compensate survivors if an on-the-job injury results in the death of a worker.

Once employees accept workers' compensation benefits, they cannot sue their employer unless there is proof that the employer knew about the unsafe condition causing the accident and did not do anything to fix it.

In some states, small businesses are exempt from workers' compensation requirements, and employees working for them are not covered. Also, business owners, independent contractors, occasional workers, domestic workers in private homes, agricultural workers, and unpaid volunteers are not covered by workers' compensation in some states.

Employers must notify employees of their right to compensation for work-related injuries and diseases. Employees must also be notified that they cannot be fired for filing a claim and that workers' compensation premiums cannot be deducted from their pay. Most employers display a poster in the workplace containing this information.

COVERAGE PROVIDED BY WORKERS' COMPENSATION Medical expenses for employees injured on the job should be covered by workers' compensation. If an employee is out of work for more than a few days, a percentage of lost wages may also be covered. Lost wage payments are usually about two-thirds of the employee's income, not to exceed state limits. If an employee is left permanently disabled from a work-related injury, the employee may be eligible for a lump-sum payment or long-term benefits. This depends on whether the employee can perform other work that pays as well as the former position. If a worker cannot earn as much as before, the worker may be eligible for a long-term payment. If the worker is completely and permanently disabled, the worker may be eligible for Social Security benefits.

INJURIES NOT COVERED Although laws vary from state to state, generally, the following injuries would not be covered by workers' compensation insurance:

- Injuries individuals afflict on themselves
- Injuries suffered under the influence of alcohol or illegal drugs
- Injuries suffered during a fight that the injured employee started
- Injuries suffered while disobeying orders or violating employer policy
- Injuries suffered while committing a crime
- Injuries suffered while not on the job



FILING A CLAIM There are certain steps that must be followed in the event of an injury or illness at the workplace. Be sure that you are familiar with these steps so that you know what you and your employee should do in the event of an accident at your business.

1. **The injured employee must notify the employer.** The employer must be notified immediately after the accident. Check your state law to determine the time limit that employees have for reporting an accident or illness.
2. **The employee must follow doctor's orders.** If the employee does not follow the doctor's orders, it could be grounds for denying workers' compensation coverage. The doctor should put any special requirements for the employee in writing. Be sure the employee goes to the doctor that handles the workers' compensation cases for your business.
3. **The employee must file the claim.** The employer must provide the employee with the proper forms, but it is the employee's responsibility to file the claim.

Checkpoint

What is the purpose of workers' compensation insurance?

Risks in International Business

When you start working with businesses and customers in other countries, there are other risks that you face. If you ship an order without receiving payment first, you risk never being paid for the order. It will be much more difficult for you to collect the payment from a business in another country. Businesses in other countries may want to pay you with their country's currency. You will have to consider the stability of the value of their currency against the American dollar before agreeing to payment terms.

Doing business in a foreign country can be difficult. You will encounter problems that you probably have not run into in the United States. These new challenges will arise for several reasons.

1. **You may not speak the language of the countries you are targeting.** If you cannot communicate with buyers or consumers, how can you sell your service or product? Misunderstandings are likely to occur.
2. **You may not be familiar with the laws, customs, and cultures of foreign countries.** In the United States, looking directly at people while speaking to them is a sign of respect. In some other countries, it is a sign of disrespect. If you fail to recognize these differences, you risk offending those with whom you are trying to do business.
3. **You may have to change your products or services to meet the needs of new markets.** Consumers abroad have different needs and wants than do consumers in the United States. What sells in this country will not necessarily appeal to foreign customers. You will need to consider this when you sell products or services in other countries.



4. **Your travel and shipping expenses may be high.** International flights can be very expensive. Sending or receiving packages overseas can also be costly.

Strategies for Dealing with Global Risks

If you decide to conduct business globally, you should develop a plan that outlines your goals and identifies your risks. Analyze the foreign target market and perform research to learn more about the risks of doing business abroad. Strategies recommended for dealing with the risks of international business include the following:

1. **Seek government assistance to answer your questions about international business.** Government agencies such as the Small Business Administration and the International Trade Administration can provide counseling, locate buyers overseas, and promote U.S. products and services.
2. **Conduct business in many different countries.** If you are doing business in only one country and something happens in that country, such as political upheaval, you run the risk of losing all sales and profits.

Famous Entrepreneur

Merv Griffin

A legend in his own time, the late, great Mervyn Edward Griffin Jr. has left his mark on the world. Griffin was not afraid to take risks during his career. He built a very successful empire because of the chances he took. *Wheel of Fortune* and *Jeopardy* are the creations of Merv Griffin. He even wrote the *Jeopardy* theme song.

Griffin was multitalented as a singer, musician, actor, and television talk-show host. His game-show empire landed him on the *Forbes* list of the richest Americans. When he sold the rights to his shows to Columbia Pictures Television for \$250 million, he was not interested in retiring. He went into real estate and other ventures to escape boredom.

Griffin's talents were evident early in his life. His Aunt Claudia taught him to play piano at age 4. Soon he was staging shows on the

back porch of the family home. He had a show every Saturday, recruiting the neighborhood kids to join him. He thought of himself as a producer even then, assigning them to be stagehands, actors, the audience, or all three!

He quit college and got a \$100-per-week job as a singer on the radio. His career in the entertainment field began there. He was introduced to game shows in New York and hosted several.

Merv continued working until he died in August 2007. His son Tony summed up his life by saying, "He loved business and continued his many projects and holdings even while hospitalized."

Think Critically

What moves in Griffin's career do you think were risky for him?



© Authenticated News/Getty Images

Why do you think creativity is an important attribute for entrepreneurs?



3. **Work with local business partners.** If you partner with a company that is located in the country you are targeting, your company will be better received by locals in that country.
4. **Employ local management.** If you hire managers from the country you are targeting, they will have a better understanding of the cultural and political scene of the country. They will be able to assist you in any product modifications or changes in business practices you need to make to work with the foreign market.
5. **Learn about the other country's culture.** Research the country's cultural customs and beliefs. Develop cultural sensitivity.

Checkpoint

What are some of the challenges of competing internationally?

12.3 Assessment

THINK ABOUT IT

1. What are the risks involved in using and extending credit?
2. Why are some workplace injuries not covered by workers' compensation insurance?
3. What are some strategies you can use to reduce the risks involved with international business?

MAKE ACADEMIC CONNECTIONS

4. **COMMUNICATION** You witnessed a serious accident at your business. You need a detailed description of the accident for your insurance company. Write an account of the accident using clear, concise language. You must be objective about the accident and should not include your opinion about what happened.
5. **MANAGEMENT** You are planning to open a retail store that will sell home appliances and furnishings. Decide what type of consumer credit you will offer and develop a credit policy. Present your decisions to the class.



TEAMWORK

Discuss the following. Many employers think workers abuse workers' compensation insurance. They may hire people to investigate workers who are on medical leave to determine if they are conducting themselves in any way that is not consistent with the injuries they have claimed. Suppose a worker claims he has hurt his back and cannot work. If he is seen lifting heavy objects or climbing a ladder at his home, then the employer may have a case for discontinuing the employee's workers' compensation claim. Do you think it is ethical for employers to spy on employees? What can be done to keep workers from abusing workers' compensation insurance?



Sharpen Your Entrepreneurial Skills

Respect Cultural Diversity

In today's global economy, you will come in contact with all kinds of people. Many of these people will be from cultures different from your own. You may work with people of different cultures. You may also buy from and sell to people of different cultures. As an entrepreneur, you need to appreciate different cultures for the following reasons:

- You need to be comfortable with your customers. If you are open to other cultures, you can attract more customers.
- People from different cultures may have different needs and wants. Understanding these can help you market your business more effectively.

How can you develop good relationships with everyone you do business with? There are at least five things you can do to enhance these relationships:

1. **Avoid stereotyping people.** Don't assume that all people from a particular ethnic or cultural group hold the same values and opinions, behave the same way, or like the same things.
2. **Focus on similarities rather than differences.** Most people, regardless of their culture, want the same things in life.
3. **Learn about different cultures.** Learning about a different culture will make you more comfortable around people from that culture. Learn how people in a different culture live and work.
4. **Make friends with someone from a different culture.** The friendship will help you begin to appreciate other cultures.
5. **Try to understand and identify with other people's feelings.** Try to see the world through the eyes of people from different cultures. Try to understand cultural views that are different from your own.



© PhotoDisc/Getty Images

TRY IT OUT

Before conducting business in another country, you will have to answer many questions to address the risks. Will your product sell well in another country or will you have to make modifications to it? What aspects of the country's culture could affect your business? How can you learn about another country's culture? Using the Activity CD, open the activity "Competing in the Global Economy." Print a copy and complete the activity.



Chapter 12 | Assessment

SUMMARY

12.1 Business Risk

1. To prepare for risks, you should (1) determine what can go wrong, (2) develop a plan, and (3) communicate your plan to employees and first responders.
2. Theft is one of the biggest risks faced by business owners. Types of theft include shoplifting, employee theft, robbery, credit card fraud, and bounced checks. Business owners can take precautions to prevent these risks.

12.2 Insure Against Risks

3. Classifications of risk faced by businesses are based on the result of the risk (pure or speculative), controllability of the risk (controllable or uncontrollable), and the insurability of the risk (insurable or uninsurable).
4. Insurance does not cover risks that cannot be reasonably predicted or if the financial loss cannot be calculated. Uninsurable risks are tied to economic conditions, consumer demand, competitors' actions, technology changes, local factors, and business operations.
5. You will have to analyze the risks your business faces to determine the types of insurance you should purchase. A typical business owner's policy (BOP) covers property damage, business interruption, and liability. Depending on your situation, you may also want to purchase life, flood, crime, or renter's insurance.
6. Before committing to an insurance purchase, compare prices and policies and seek advice from experienced business owners.

12.3 Other Risks

7. Although useful to you as a business owner and your customers, credit has risks associated with its use. You must analyze the potential risks of credit to determine if it is wise for you to use and/or accept it.
8. Workers' compensation insurance covers employees' medical expenses and lost wages incurred as a result of workplace injuries and occupational illnesses.
9. To reduce international business risks, companies should seek government assistance, conduct business in many countries, involve local business partners, employ local management, and learn about the culture.

What do you know now?

Read Ideas in Action on page 331 again. Then answer the questions a second time. How have your responses changed?

VOCABULARY BUILDER

Match each statement with the term that best defines it. Some terms may not be used.

1. The possibility of some kind of loss
2. Taking action to prevent or reduce the possibility of loss to your business
3. Looking at all aspects of your business and determining the risks you face
4. The act of knowingly taking items from a business without paying
5. A payment to cover the cost of insurance
6. A risk that presents the chance of loss but no opportunity for gain
7. A risk on which actions have no effect
8. A pure risk faced by a large number of people and for which the amount of loss can be predicted
9. When one business allows another business to buy now and pay later
10. A law that provides for benefits to employees who have suffered work-related injuries or occupational diseases
11. A risk that can be reduced or possibly even avoided by actions you take
12. A risk that presents the chance to gain as well as lose from an event or activity

- a. bounced check
- b. consumer credit
- c. controllable risk
- d. Federal Employees' Compensation Act (FECA)
- e. insurable risk
- f. premium
- g. pure risk
- h. risk
- i. risk assessment
- j. risk management
- k. shoplifting
- l. speculative risk
- m. trade credit
- n. uncontrollable risk

REVIEW YOUR KNOWLEDGE

13. **True or False?** Businesses can avoid all possible risks by purchasing insurance.
14. Conducting a risk assessment involves all the following actions *except*
 - a. learn the risks your business faces
 - b. decide how risks will affect your business
 - c. prioritize the risks by the impact they will have on your business
 - d. communicate your plan
15. **True or False?** Credit card fraud is an example of an economic risk.
16. If there is a risk that a loss will occur and the amount of the loss cannot be predicted, the risk is ___?___.
17. **True or False?** A credit card offered by a home furnishings center is an example of an installment loan.
18. Which of the following is *not* a risk associated with doing business in another country?
 - a. language barriers
 - b. different laws, customs, and cultures
 - c. high travel and shipping costs
 - d. all of the above are risks
19. A ___?___ plan will enable you to get back to business as quickly as possible after a disaster and help you continue to meet customer needs.

20. Which of the following types of insurance would cover the cost to repair your office building if it were damaged by fire?
 - a. property insurance
 - b. business interruption insurance
 - c. liability protection
 - d. life insurance
21. A change in the way web sites are accessed that requires new, expensive computer equipment is an example of a risk related to
 - a. economic conditions
 - b. consumer demand
 - c. competitors' actions
 - d. technology changes
22. Which of the following types of insurance would cover losses your business incurred as a result of selling a faulty product that injured someone?
 - a. property insurance
 - b. business interruption insurance
 - c. liability protection
 - d. life insurance
23. **True or False?** A speculative risk is classified as uninsurable.
24. **True or False?** The credit that a retail business extends to customers is called trade credit because they are trading money for goods.
25. **True or False?** When you extend credit to a customer, you are guaranteed that you will receive payment for the goods or services sold.
26. **True or False?** All injuries that occur at work are covered by workers' compensation insurance.
27. Which of the following is *not* a strategy for dealing with a global risk?
 - a. conduct business in only one country to minimize the risk
 - b. seek government assistance
 - c. work with local business partners
 - d. employ local management
28. **True or False?** If you are leasing a building for your business, you do not need to carry renter's insurance because the owner of the building is required to carry insurance.

APPLY WHAT YOU LEARNED

29. You plan to open a horseback riding training center with a horse boarding facility. Make a chart and list the types of risk you will face. Categorize the risks as human, natural, or economic. Classify risks as controllable or uncontrollable and insurable or uninsurable. If the risk is insurable, list the type of insurance that you could purchase to protect against the risk.
30. Make a list of accidents and injuries that workers in a hospital could experience. Write "yes" next to the accidents and injuries that will be covered by workers' compensation insurance. Write "no" next to those that would not be covered.
31. You own a clothing boutique and have recently expanded into catalog sales. Many of your products will be sold abroad. What cultural issues are relevant to your business?

MAKE ACADEMIC CONNECTIONS

32. **MATH** You are trying to decide whether to purchase security equipment for your business or hire a security guard. You research the cost of the security equipment you will need and find that it will cost \$15,000 and has a useful life of 3 years. You have looked into hiring a security guard through an agency and find that it will cost you \$50 per hour to hire a guard for 3 hours per day. Calculate and compare the annual cost of each and decide which will be the most cost-effective for your business.
33. **COMMUNICATION** Interview a business owner in your community to find out what type of controls the owner has in place for handling cash to minimize losses due to theft. Prepare a presentation and share your findings with the class.

WHAT WOULD YOU DO?

Your business is growing and you recently hired five new employees. Your business has been exempt from paying workers' compensation insurance premiums, but with the addition of new employees, you will no longer be exempt. You do not agree with the workers' compensation program because of the added expense to your business. You are thinking about not paying the premiums. Would this be fair to your employees? What would happen if one of your employees had a serious injury on the job and you did not have workers' compensation insurance?



BUILD YOUR Business Plan *Project*

This activity will help you continue with the development of a business plan by outlining your risk management plan.

1. Identify risks faced by your business and establish a plan for dealing with them. Describe how the business will prevent shoplifting, employee theft, robberies, credit card fraud, and bad checks. Research how much it will cost to buy special security equipment or hire a guard. Present your proposal to the class. Prepare to defend your strategies.
2. Contact an insurance agent to obtain information on insuring your business. What types of insurance do you need? How much coverage should you buy?
3. Research workers' compensation laws for your state. Explain how you will meet your responsibilities for these laws.
4. What are some other cultures you will be exposed to in your business? Research one of these cultures and find out information about the lifestyle and business practices associated with this culture. What cultural issues will affect your business? How will you market your product or service to this and other cultures?



Planning a Career in Insurance



"After returning from the grocery, our neighbor came home to a big mess. The laundry he had tossed into the machine prior to leaving the house had been off-balance. During the spin cycle the water hose became loose and caused a huge water leak. Although he did his best to dry out the floors, he ultimately had to replace the hardwood flooring in the rooms bordering the laundry room. Fortunately his homeowners insurance covered the costs."

How do individuals and businesses protect their assets from unexpected mishaps that result in financial expenses? How is insurance coverage matched to particular levels of need?

Insurance agents sell and service insurance policies. The agent is an intermediary between the insurance provider and the insurance buyer. Agents are responsible for explaining policies to clients and helping them obtain appropriate coverage for specific situations.

EMPLOYMENT OUTLOOK

- Slower than average growth is anticipated.
- As insurance is a basic societal requirement, there will be a steady need for agents.
- Agents who utilize both Internet efficiencies and automated claims processing should be able to expand their client base.

JOB TITLES

- Career Agent
- Financial Services Agent
- Licensed Sales Professional
- Agency Specialist
- Property & Casualty Underwriter
- Strategy Director, Protection Business

NEEDED SKILLS

- As insurance policies are complex, a Bachelor's degree, with a business or mathematics focus, is often required.
- A state license is required to sell insurance.
- Professional certification is available to demonstrate competency in specialized areas.
- Continuing education is often mandatory.

What's it like to work in Insurance

Narelle, an independent insurance agent, is comparing automotive insurance policies from a variety of policy providers for her new client—a young driver. As an independent agent, Narelle matches the needs of her clients to the policies that provide the best combination of rates and coverage. Narelle knows that by providing her young client with economical, effective coverage as well as courteous service, she can probably secure him as a new long-term client.

After lunch, Narelle finishes the handouts she is preparing for tomorrow's lunch seminar at a local Small Business Administration meeting. She is planning to discuss the appropriate types of coverage for each stage of business development. Narelle has learned that participation in professional meetings often results in valuable sales leads. As an independent agent, developing new clients is essential to her ongoing success.

What about you? Would you like to help individuals and businesses identify their risks and help them obtain the appropriate insurance coverage to protect their assets?



BUSINESS SERVICES MARKETING SERIES EVENT

Lincoln is a national award winning city that takes great pride in its landscaping. Beautiful Spaces is a landscaping company owned by one of the Lincoln city council members (Chris). Beautiful Spaces has contracted with Lincoln for the past several years to plant, mow, water, and maintain the medians. The company has a \$400,000 annual contract for its landscaping services.

Lincoln residents have not been happy with the work performed by Beautiful Spaces. The medians are not maintained, and many projects are incomplete. Beautiful Spaces has blamed its delays on bad weather, a low supply of water, and a shortage of flowering plants.

You are the city manager for Lincoln. You must meet with Chris to let him know that the city will not honor the contract with Beautiful Spaces because the company has not fulfilled its commitment. You must also work out an acceptable financial agreement that takes into account the inadequate and incomplete work. Based on the schedule outlined in the contract, Beautiful Spaces should have completed the project 60 days ago. The contract states that a \$100 fine will be charged for each day of incompleteness. Beautiful Spaces has been paid \$150,000 for completion of one-fourth of the total project. You will meet with Chris to discuss an acceptable agreement for ending the contract and paying the city fines for incomplete work. You have ten minutes to determine your plan of action and ten minutes to explain your plan to the owner of Beautiful Spaces. Chris (the judge) can ask questions about your plan of action following your presentation.

PERFORMANCE INDICATORS EVALUATED

- Describe legal issues affecting businesses.
- Describe the nature of legally binding contracts.
- Demonstrate responsible behavior.
- Demonstrate honesty and integrity.
- Explain business ethics in product/service management.

Go to the DECA web site for more detailed information.

Think Critically

1. What is the conflict of interest in this case?
2. Why should Beautiful Spaces pay the city of Lincoln?
3. What compromise could the city propose to reduce the fines?
4. How can the city avoid this situation in the future?

www.deca.org

Chapter 13

© Digital Vision/Getty Images



Management for the Future

13.1 Growth Strategies

13.2 Ethical and Social
Issues

13.3 Global Trends and
Opportunities

school.cengage.com/entrepreneur/ideas

IDEAS IN ACTION

Starting Young and Moving Up

Joseph Pascaretta is a motivational speaker, private pilot, college student, and successful entrepreneur. He started his first business at the age of 11. Because of his young age, he faced many obstacles in establishing professional relationships. Members of the business community did not want to take him seriously.

His first business was a web design company that he started with his friend, Aaron Downen, who was the web designer. Joseph sold the web services to local businesses, including a car dealership, and Aaron built the web sites. The business grew steadily until 2003, when the market for web design services changed. So, Joseph changed the business and began to offer database integration services. His company, Alps Technology, purchased 3-million gigabytes of database service space and began offering its clients full-service database integration, including IT support, database space, software consulting, and hardware integration. Today, Alps Technology employs 44 people, and most of these are college students who work from home. Joseph learned at an early age that success is about what you do differently.

In 2002, Joseph was looking for a way to invest revenue from Alps Technology into another profitable business. He purchased a commercial lawnmower and began to offer landscaping services. Today, Alps Lawn Company has a client base of 60 residents and 21 businesses and has plans to expand into three other states. To visually show clients what their landscape project will look like, Joseph uses computer-aided design landscape software. He integrates his interest in flying into the business by offering aerial photography of the landscaping projects.

Joseph attends the University of Michigan while continuing to run his two businesses. With two successful businesses already up and running, Joseph could have decided to skip college, but he realized that a college degree is a valuable asset in today's business world. After college graduation, he plans to evaluate his options and see what opportunities are available. As an entrepreneur, he is always looking for new, innovative ways to reestablish himself in the business world.



© Joseph Pascaretta

Joseph Pascaretta, Alps Technology and Alps Lawn Company

What do you know?

1. How do you think Joseph knew when to add new services to his web design business?
2. Why is it important for Joseph to continue to offer new services to his customers?
3. Why do you think business owners need to be aware of what is going on in the business world and be willing to change when necessary?

13.1

Growth Strategies

Goals

- Determine when a business is ready to expand.
- Explain the importance of planning for growth.
- Identify and describe three growth strategies.
- Describe the product life cycle and product development stages.

Terms

- market penetration
- market development
- product life cycle
- prototype

Focus on Small Business

Know when to grow

Mary Ardapple, owner of Apple's Bakery in Peoria, Illinois, has moved her business three times since she opened it in 1989. Her menu has expanded and now has three times its original offerings. She even makes her baked goods available to those outside the Peoria area through an online store.

Mary is not content to conduct business as usual and is always looking for new opportunities. Currently, she is planning to add a health-conscious line of baked goods to her offerings. Throughout all the moves and expansions, Mary and her team have not forgotten the company's original motto, "Where smiles are made from scratch!"

Work as a Team How do you think Mary has known when her business was ready to expand? Do you think it is important for Mary and her team to always remember their original motto?



© PhotoDisc/Getty Images

Business expansion should be carefully planned.

Determine When to Expand

Sooner or later, you will consider expanding your business. Some businesses have difficulty growing. Others expand too quickly. To expand successfully, you will need to determine both when and how to expand. You will also need to control your growth.

Before deciding to grow your business, be sure that all of your operations are functioning well. Unresolved operational issues will only get bigger and cause more problems when the business gets larger. You also need to be sure that you take care of your current customers when you begin growing your business. Remember, they helped you get where you are. You want them to feel comfortable

with the changes, knowing that their needs will continue to be met.

Determining when to expand depends on two main factors: the condition of your business and the economic conditions in the market in which your business competes.

Consider the Condition of Your Business

How do you determine when it is time to expand your business? Some of the signs you should look for include the following:

- Your business is recognized by your community and industry.
- Your sales are rising.
- You have a customer base that regularly buys from you.
- You are hiring more employees and now have managers.
- You need more space.

Assess Economic Conditions

If the condition of your business shows that you should expand, you should next analyze the economic climate that controls the business. You should ask the following questions:

1. How is the national economy doing? Are people worried about spending money, or are they spending freely?
2. What are the economic conditions in your industry or region?
3. Have the demographics of your market changed?
4. Is demand for your product or service expected to remain strong?
5. Does your business face new competition?

Checkpoint

What factors should you consider before deciding to expand your business?

Control Your Growth

Growing rapidly may sound like a great thing for a business, but uncontrolled growth may be just as bad as no growth at all. Businesses that grow too quickly often find that they don't have the resources to support their growth. They can lack money, employees, supplies, and more. As a result, they often overextend themselves. Sometimes they are even forced to go out of business.

Joshua King owned a successful bookshop, Pegasus Books. Excited over his success, Joshua opened a second shop, but he underestimated the costs involved in running a second store. The stress of managing two stores was overwhelming, and Joshua found he could no longer provide the personal service his customers wanted. After nine months, Joshua had to close his second bookstore.

★ Develop Your Reading Skills

While reading, write notes highlighting the main ideas. At the end of each section, review what you have written and fill in any gaps. Focus on the important points, and support them with relevant details.



Create a Plan for Growth

To make sure that your business expands successfully, you will have to control its growth. This means you will need to come up with a plan for expansion that should include strategies for the following:

- attaining measurable objectives and goals (examples are reaching sales goals, increasing your customer base, and opening another store)
- hiring managers and supervisors
- financing expansion
- obtaining resources for expansion (capital, equipment, inventory, materials, and supplies)

Checkpoint

Why is it important to control the growth of your business?

Choose a Growth Strategy

You can expand your business in various ways. You can get more people to buy your products or services. You can expand into other geographic areas. You can also find new products and services to sell.

WHAT WENT WRONG



Makeup Test

Sarah-Jane Stevens founded Charisma Cosmetics. Her company targeted professional cosmetics dealers serving makeup artists in the film, TV, and theater industries. Charisma Cosmetics had an excellent reputation as a high-quality manufacturer, a loyal customer base, and a major share of the market. However, competitors were slowly chipping away at Charisma's customer base. To remain competitive, Sarah-Jane rolled out a new brand, Picture-Perfect by Charisma, in the fall of 1999. This brand was specifically designed to be sold in department stores.

The new strategy angered the professional cosmetics dealers who were the core customers of Charisma Cosmetics. Their competitive advantage had been to provide better products that were not available elsewhere. With Charisma's Picture-Perfect brand on the market, they no longer had the same competitive edge.

"We were determined to grow, and we strayed from our root value of 'don't be bigger, be better,'" Sarah-Jane said. Just eight months after getting into the department store market, Sarah-Jane got out. The company ended up losing hundreds of thousands of dollars in developing and marketing the Picture-Perfect brand.

Think Critically

1. What problems were created by the "Picture-Perfect by Charisma" brand?
2. How might Sarah-Jane have expanded without angering her dealers?



© PhotoDisc/Getty Images

Consider the risks when growing your business.

Penetrate the Market

Market penetration is increasing market share for a product or service within a given market in a given area. If total sales for your target market are \$500,000 and your business attracts 5 percent of that market, your sales will be \$25,000. If you raise your market share to 15 percent, your sales will be \$75,000.

You can increase your market share by doing the following:

- Increase your advertising.
- Offer customers special deals, such as frequent-buyer cards, incentives to purchase, and discounts.
- Offer superior customer service.

Taking these actions will cost you money. You may spend more on advertising or incur the cost of giveaway items. But spending money now can pay off with larger profits in the future.

Expand Geographically

Geographic expansion occurs when you decide to market your service or product in another town, city, county, state, or country. Sheila Velez owns a business that builds sunrooms in the northern part of her state. To increase sales, Sheila recently began advertising throughout the entire state. She has already received calls from consumers 100 miles away who are interested in her product.

Diversify with New Products or Services

Market development is a strategy for expanding the target market of a business. A business expands its target market by diversifying, which means selling new products or services in addition to what it already offers.

Sue Ann Rader owns a musical instrument store. Three years ago, she added a sheet music department. She reduced the inventory of instruments to make room for the inventory for the new department. Sheet music now contributes 25 percent of her annual profits.

Businesses can fail if they diversify into the wrong areas. Use the following guidelines to make sure that your business diversifies successfully.

- Do not go into areas that you know nothing about.
- Choose a product or service that complements what you already sell.
- Avoid investing too much capital in new areas before you know if they will be profitable.
- Don't neglect your original product or service line.

Sue Ann would like to open a cafe in her store. She would have to make room in her store to do so. Her lack of experience in running a cafe and her concern about the effect on her main business convince her not to open it.

Checkpoint

What are some ways you can expand your business?



Product Life Cycle and Development

A business must constantly monitor the sales of products and develop new products. Consumer interest in most products will decline over time. A business must keep developing new products in order to maintain a presence in the market.

Stages of a Product Life Cycle

The stages a product goes through from the time it is introduced to when it is no longer sold is called its **product life cycle**. A product goes through four stages in its life cycle: introduction, growth, maturity, and decline. The stage of the life cycle can be determined by the type of competition the product is facing.

INTRODUCTION The first stage of the product life cycle is the introduction of a new product into the market. At this stage, the product is quite different from existing products, so customers are not aware of it or how it can satisfy their needs. The price may be high during this stage as the company tries to cover the expenses of developing the product. The competition, if any, for the product at this stage consists of older, established products.

GROWTH If a product is successful in the introductory phase, it will attract more customers and enter the growth stage as sales begin to increase. The product will be distributed more widely as more consumers start to buy it. Competitors will see the opportunity for sales and introduce their own product. A competitor's product needs to have different features and options so that it can be positioned in the market as a better product. There will be a wider range of prices for the product during this stage due to competition.

MATURITY During the maturity stage of the life cycle, sales peak and profits begin to decline. The product is in high demand and many companies offer it, so competition is very intense. Pricing becomes an important factor at this stage, since customers view products on the market as being similar. Businesses will offer discounts or sale prices to encourage customers to buy their brand. Companies make sure their product is easy for customers to find. During the maturity stage, a great deal of money will be spent on promotion, because companies want to keep their brand of the product on the minds of customers.

DECLINE The decline stage occurs when consumers decide that a product is no longer meeting their needs or when they discover new and better products. Sales will begin to drop rapidly, and profits will drop. During this stage, there is little opportunity for product improvement. Since the product is not contributing a profit, no more money will be invested in it. Distribution is cut to only areas where the product is still profitable. Many times the price is cut during the decline stage. Promotion is decreased and targeted specifically to loyal customers in an effort to keep them as long as possible.



New Product Development

In order to stay competitive in the market, a business must develop new products or services to offer to customers. When a business decides to develop a new product, it takes steps to be sure that it develops a product that is likely to be successful. The business wants to find out early in the development process whether the product is likely to be successful before investing too much money in it. It is also important for the business to determine that the product meets an important market need, can be produced well and at a reasonable cost, and will be competitive with other products in the market. Soft drink companies introduced more new products during 2000-2002 than were introduced during the entire decade of the 1990s. New soft drink products continue to be introduced each year.

SOFT DRINKS INTRODUCED SINCE 2000			
Drink	Company	Drink	Company
Introduced in 2007 Diet Pepsi Max	Pepsi Cola	Introduced in 2002 Vanilla Coke	Coca-Cola
Introduced in 2006 Coca-Cola BlaK	Coca-Cola	Diet Vanilla Coke	Coca-Cola
Introduced in 2005 Coca-Cola Zero	Coca-Cola	Dr Pepper Red Fusion	Dr Pepper/7 UP
Coca-Cola with Lime	Coca-Cola	dnL	Dr Pepper/7 UP
Mountain Dew MDX	Pepsi-Cola	Pepsi Blue	Pepsi-Cola
Pepsi Lime	Pepsi-Cola	Diet Mountain Dew Code Red	Pepsi-Cola
Introduced in 2004 Diet Coke with Lime	Coca-Cola	Sobe Mr. Green	Pepsi-Cola
Coca-Cola C2	Coca-Cola	Introduced in 2001 Diet Coke with Lemon	Coca-Cola
Introduced in 2003 Mountain Dew Livewire	Pepsi Cola	Fanta (reintroduced in U.S.)	Coca-Cola
		Diet Sierra Mist	Pepsi-Cola
		Mountain Dew Code Red	Pepsi-Cola
		Mountain Dew AMP	Pepsi-Cola
		Introduced in 2000 Pepsi Twist	Pepsi-Cola
		Diet Pepsi Twist	Pepsi-Cola
		Sierra Mist	Pepsi-Cola
		Red Flash	Coca-Cola

Product development involves the following steps: (1) idea development, (2) idea screening, (3) strategy development, (4) financial analysis, (5) product development and testing, and (6) product marketing.

IDEA DEVELOPMENT The first, and often the most difficult, step in product development is finding ideas for new products. Employees or customers can generate ideas. Many times salespeople will hear wishes and complaints from customers about what they would like to see and not see in products. If the salesperson shares this information with the development department, this can help with ideas for new products.

IDEA SCREENING Once ideas have been developed, they are screened to select the ones that have the greatest chance of being successful. Questions to be answered during the screening process include the following:

- Has a market been identified for the product?
- Is the competition in the market reasonable?



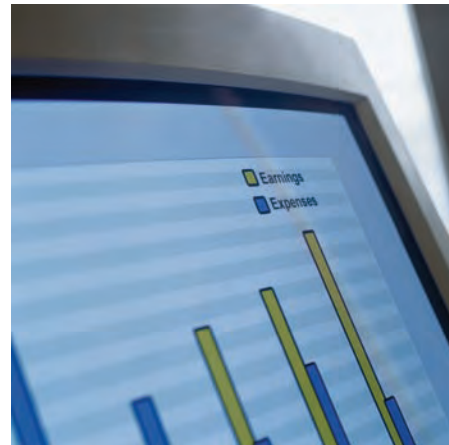
- Are resources available to produce the product?
- Is the product legal and safe?
- Can a quality product be produced at a reasonable cost?

STRATEGY DEVELOPMENT Once an idea has been determined to be reasonable, the business will create and test a sample marketing strategy. The business performs research to identify the appropriate target market and to be sure that there are customers with adequate income who are looking to satisfy a need that the product meets. Questions asked during this stage include:

- What is the likely demand for the product?
- How would the introduction of the product affect existing products? Would the new product take away market share from existing products the company produces?
- Would current customers benefit from the product?
- Would the product enhance the image of the company's overall product mix?

FINANCIAL ANALYSIS If a new product idea is determined to meet a market need and can be developed, the company will perform a financial analysis. Spreadsheet programs are often used in this step. Costs of production and marketing, sales projections for the target market, and resulting profits are calculated. Questions to be answered at this stage include the following:

- What impact could the new product have on total sales, profits, market share, and return on investment?
- Would the new product affect current employees in any way? For example, would it require people with different skills, the hiring of more people, or a reduction in the size of the workforce?
- What new facilities, if any, would be needed?
- How might competitors respond?
- What is the risk of failure? Is the company willing to take the risk?



Why is it necessary to perform a financial analysis when developing a new product?

PRODUCT DEVELOPMENT AND TESTING When a manufacturer sees a market opportunity and decides to develop a new product, it makes a **prototype**, which is a full-scale model of a new product. After testing the prototype in the laboratory and making final adjustments, the company designs the production process, obtains needed equipment and materials, and trains production personnel. The product is then test-marketed in selected areas. If it receives a positive response, the manufacturer places the product into full production. If not, the manufacturer drops it.



PRODUCT MARKETING Introduction of the product into the target market is the last step in the product development cycle and the first step of the product's life cycle. Before this takes place, many other things must be done. The marketing mix elements must be carefully planned, and there must be an adequate supply of the product on hand to meet the needs of the target market.

Once the product has been introduced into the market, the company will have to monitor its life cycle. Many new products fail even though the product development steps have been followed carefully. Products may not match the needs of customers, or customers may not see what differentiates the product from other products on the market. The product may be priced too high or too low, poorly distributed, or improperly promoted.

Checkpoint

Why must a business be concerned with the life cycle of a product and with new product development?

13.1 Assessment

THINK ABOUT IT

1. What are the negative consequences, if any, of not allowing your business to grow?
2. What are some ways you can control the growth of your business?
3. Your friend owns a successful hair salon. She wants to expand and asks for your advice on a growth strategy. What will your advice be?
4. List the stages of the product life cycle, and provide an example of a product in each stage.

MAKE ACADEMIC CONNECTIONS

5. **MATH** Tony Balducci owns a deli and sandwich shop. Total sales for his target market are \$1.75 million per year. If he attracts 12 percent of the market, what will his sales be? What will sales be if he increases market share to 18 percent?
6. **MATH** Luis Zapata owns a sports center with an indoor track, driving range, and basketball courts. He has recently installed two batting cages at the facility. Last year, his total sales were \$325,500. If the batting cages take up 5 percent of the space and add 4 percent to total sales, how much will each batting cage contribute to total sales?



TEAMWORK

Form teams. List examples of business growth that you have seen. Classify the examples as market penetration, geographic expansion, or market development.



13.2

Ethical and Social Issues

Goals

- Define ethics.
- Recognize the need for ethical practices in business.
- Discuss an entrepreneur's social responsibilities.
- List ways to meet a business's environmental responsibilities.

Terms

- ethics
- code of ethics
- business ethics

Focus on Small Business

Making a difference

Perhaps you own a "Life is Good" shirt or some other item with Jake's smiley-face stick figure on it. Bert and John Jacobs, founders of the casual clothing company Life is Good, have found the slogan to be true and want to share that feeling with others. As they started the business and it began to grow, they had to make decisions about how to grow their company while staying true to their belief in the simple pleasures of life.

When it came time to decide on an advertising campaign for the company, Bert and John decided to forego the traditional advertising route and instead invest the money to help those in need. Today the company works with a number of charitable organizations and holds a series of festivals each year in the New England area. Although it started out as a different way to spend marketing dollars, today, charitable work has become a major focus for the company.

Work as a Team What do you think about Bert and John's decision to spend their advertising dollars doing good for the community? Do you think this decision has helped their company to grow more than it would have with a conventional advertising campaign?



© Digital Vision/Getty Images

Businesses have a social responsibility.

What is Ethics?

Ethics is the study of moral choices and values. It involves choosing between right and wrong. Behaving ethically means behaving in an honest and fair manner. As the owner of a business, you will have to make ethical decisions about the way you want to run your business. Thinking about ethical issues in advance will help you handle conflicts when they arise.

Culture and Ethics

Different cultures define ethical behavior differently. In some countries, it is considered unethical to take bribes. In other countries, paying bribes



© PhotoDisc/Getty Images

Why is it important for a business owner to be aware of culture and ethics when conducting business internationally?

may be an accepted business practice. In some countries, employers may treat employees badly. In other countries, employees have established rights that employers are expected to respect.

Codes of Ethics

Even within the same culture, individuals develop different standards, or codes, of ethics. A **code of ethics** is a set of standards or rules that outlines the ethical behavior demanded by an individual, a business, or a culture. Some individuals have very high standards of ethics and do what is right in every situation. Other individuals do not develop a standard of ethics at all. They act without thinking whether their actions are right or wrong.

Jan Sommers has a high personal code of ethics. Last week, she received a duplicate refund check from one of her suppliers. Jan knew that the check had been sent to her by mistake. She immediately called the supplier to report the error.

Checkpoint

What does it mean to have a high code of ethics?

Ethics and Business

Ethical questions arise in every type of business. Large corporations, small companies, and home-based businesses all deal with ethical dilemmas at one time or another. **Business ethics** is the application of the principles of right and wrong to issues that come up in the workplace.

Set High Standards

Business and ethics used to be considered unrelated to each other. Over the past hundred years, this view has changed dramatically. Businesses today recognize that they must behave in an ethical manner.



MYTHS ABOUT BUSINESS AND ETHICS Some people believe that entrepreneurs need not concern themselves with ethical issues. They believe that their only goal should be increasing profits. They may treat someone or another business unfairly and use the excuse that “it is just business.” They might think that acting ethically can hurt their profits. But in fact, using ethics in business can help you avoid disasters. It can also make customers and suppliers more willing to do business with you.

CONSUMER AWARENESS

Both consumers and business owners are sensitive to business ethics. Because consumers are so aware of ethical issues, businesses find ways to show customers that they practice ethics in their daily operations. Manufacturers of some shampoos and cosmetics print on their packaging that they do not test their products on animals. Consumers who have strong opinions about animal rights may be more willing to purchase such products.



© PhotoDisc/Getty Images

Would you be more likely to buy products that are less harmful to the environment? Why or why not?

Establish an Ethical Workplace

As the owner of your business, it will be up to you to inspire your employees to behave ethically. You will want to establish an ethical workplace for several reasons.

1. You want to do the right thing.
2. You want to serve as a role model to others.
3. You want to be proud of the way you conduct yourself, and you want others to be proud of you.
4. Ethical behavior is good for business because it gains the trust of customers.
5. Employees are more likely to act ethically if they see the business owner acting in an ethical manner.
6. Acting ethically reduces the possibility of being sued.

CREATE A WRITTEN CODE OF ETHICS One way that you can communicate your ethical beliefs to the people who work for you is by creating a written code of ethics. Such guidelines will help you and your employees make ethical decisions.

You should create a code of ethics as soon as you begin your business. Even if you are your business's only employee, you should create a written code of ethics. You should also establish company policies and procedures to let you and your employees know how to behave in certain situations.



To create an ethical code for your business, think about ethical dilemmas that may arise and come up with solutions for dealing with them. Talk to other business owners to see what kinds of ethical problems they have encountered.

Jackie Rand owns a large discount store. Every month, salespeople from various manufacturing companies come to his company to sell their services or products. They meet with the head of the purchasing department, Ellen Chao. Last month, a manufacturing representative offered Ellen a free vacation. Not sure whether she should accept the gift, Ellen checked the code of ethics outlined in the company handbook. It clearly stated that gifts worth more than \$100 should never be accepted from manufacturing representatives. Accepting large gifts from a vendor may make an employee feel obligated to purchase from that vendor when it may not be the best choice to meet the business's needs. The guidelines helped Ellen solve an ethical dilemma.

Checkpoint

Why is it important for entrepreneurs to establish and write a code of ethics?

Social Responsibilities

As an individual, you have personal responsibilities to yourself, to your family, and to your friends. Entrepreneurs also have personal responsibilities to the people they work and deal with, to the communities in which they are located, and even to the environment. What are these responsibilities, and how can you meet them?



© PhotoDisc/Getty Images

Why do businesses have a responsibility to their communities?



Responsibilities to Customers

Your customers are your most important asset. You will need to treat them properly, or they will no longer use your services or buy your products. When dealing with customers, you should do the following:

1. **Treat all customers with respect.** No one likes to be treated badly.
2. **Be honest.** Never take unfair advantage of customers who do not know everything about the product or service they want to buy. Help your customers make good purchasing decisions.
3. **Avoid exaggerating the merits of your products or services.** Remember that customers who are not happy with what they purchase will not do business with you again.
4. **Inform customers of possible dangers of the products you sell.** Remember that this is also a legal requirement.
5. **Handle all disputes fairly.** Try to see the customer's side of an issue when there is a disagreement.



© Digital Vision/Getty Images

How does a business benefit from treating customers fairly?

Responsibilities to Suppliers

You depend on your suppliers to provide you with the goods you need to manufacture or sell your products. To make sure that you maintain good relationships with them, you will need to:

1. **Treat all suppliers with respect.** If you respect them, they will respect you.
2. **Avoid spreading rumors or incorrect information about suppliers.** Do not discuss information that is not factual with others. Rumors can damage a business's reputation.
3. **Give suppliers time to fill your order.** Try not to wait until the last minute to ask for merchandise.
4. **Handle all disputes fairly.** Try to see both sides of the issue and work out a solution that is fair to both you and the supplier.

NETBookmark

Target Corporation is an example of a company that places a high value on meeting its social responsibilities. Access school.cengage.com/entrepreneur/ideas and click on the link for Chapter 13. Browse through Target's Community pages and answer the following: What is the 5% Giving program? How much money does Target give to community organizations every week? Identify two environmentally friendly measures Target has taken recently.

school.cengage.com/entrepreneur/ideas



© PhotoDisc/Getty Images

Why does a business have a responsibility to its suppliers?

5. **Let your current supplier know the reason for your decision if you change suppliers.** This is a courtesy to the supplier as well as a good business practice. The supplier will appreciate the feedback to use in developing future competitive strategies.

Responsibilities to Creditors and Investors

Creditors and investors have shown faith in your ability to succeed. To repay them for their confidence in you, you should run your business as effectively as possible. You should also let creditors and investors know when things are not going well. Never conceal risks you are facing.

Responsibilities to Your Community

Business owners have a special responsibility to contribute to their communities. They can do so in various ways, including donating money, products, and services. They can also get involved in community issues or activities.

CONTRIBUTE MONEY Business owners should donate money to charities, cultural institutions, and causes in which they believe. It is their responsibility to give something back to the community. Not all business owners can make large contributions, but any donation is welcomed.

DONATE PRODUCTS OR SERVICES Some businesses donate the products or services their business sells. Used clothing stores donate unsold clothes to charities. Computer companies sometimes send technicians to community agencies to help the staffs learn about computers.

Carrie Rios owns a restaurant. She used to discard all the leftover food every evening. But now, Carrie donates this food to the local soup kitchen. Food that Carrie would have thrown away is enjoyed by dozens of people who otherwise might not have eaten a good meal.

did you KNOW?

According to the National Philanthropic Trust, in 2006 the five largest corporate grant-makers were:

- Wal-Mart Foundation, \$154.5 million
- Aventis Pharmaceutical Health Care Foundation, \$114.7 million
- Bank of America Foundation, \$80.7 million
- Ford Motor Company Fund, \$77.9 million
- The Wells-Fargo Foundation, \$65.0 million



GET INVOLVED You can contribute to your community in other ways as well. Some entrepreneurs get involved in issues affecting their local governments, such as changes in zoning laws and the establishment of local parks. Others get involved by sponsoring local events or organizations, such as a school sports team.

Checkpoint

What are some responsibilities entrepreneurs have to suppliers, customers, and the community?

Respect the Environment

Damage to the environment comes from many different sources. The burning of coal and oil for energy pollutes the air. Release of toxic chemicals pollutes the ground, air, and water. Disposal of billions of tons of garbage every year also creates environmental problems.

Businesses have a major impact on the environment. As an entrepreneur, you will have an obligation to do as little harm as possible to your surroundings. To meet your environmental responsibilities, you should do the following:

1. **Protect the environment from pollutants.** Don't knowingly dump hazardous material on the ground or in lakes and rivers.
2. **Conserve nonrenewable resources, such as coal and oil, by using them efficiently.** Nonrenewable resources are not easily replaced once they are gone. It takes hundreds of years to regenerate a nonrenewable resource. Use alternative resources when available.
3. **Reduce waste and dispose of waste responsibly.** Recycle materials such as paper, plastic, aluminum, glass, and steel.
4. **Use environmentally safe and sustainable energy sources to meet your business needs.** Electricity is a good example. It can be replaced quickly and is not a major source of pollution.



Would you be more likely to shop at a store that is environmentally responsible? Why or why not?

5. **Sell products that cause as little damage to the environment as possible.** For example, don't sell a car-wash solution that harms plant life.

LAWS GOVERNING THE ENVIRONMENT In 1970, the federal government created an agency to enforce the laws governing the environment. The Environmental Protection Agency (EPA) enforces federal laws concerning clean air and water. If your business handles hazardous materials, you will need to become familiar with these laws.

Checkpoint

As a business owner, what are some things you can do to protect the environment?

13.2 Assessment

THINK ABOUT IT

1. All employees should practice ethical behavior. Think of some ethical dilemmas that a convenience store clerk might encounter. Then, describe how the clerk could handle these situations.
2. Is it important for entrepreneurs to always act in an ethical manner? Why or why not?
3. Explain the concept of personal responsibility.
4. At what point do you think a business owner should tell creditors and investors of a new risk the business is facing? Why?

MAKE ACADEMIC CONNECTIONS

5. **COMMUNICATION** Using the Activity CD, open the activity "Business Ethics." Print out the case studies and work with a partner to decide the best way to handle each situation.
6. **MATH** Jade Yorida will donate 12 percent of her company's net income to the community if she makes her profit projections of a 5 percent increase over the previous year's net income of \$235,000. Assuming Jade's income does increase by 5 percent, how much will she donate?
7. **RESEARCH** There have been many cases in recent years of businesses and individuals who have not practiced ethical behavior. Research a business or individual who has been caught practicing unethical behavior and prepare a report on your findings.



TEAMWORK

Working with teammates, brainstorm five ethical dilemmas that entrepreneurs might face. Then, determine what decisions you would make if you were faced with these problems. Share your thoughts with the class.



13.3

Global Trends and Opportunities

Goals

- Discuss the reasons and methods for participating in the global economy.
- Explain how to determine whether international business is right for you.
- Identify trade regulations that affect international business.

Terms

- exports
- imports
- trade barriers
- quota
- tariff
- qualitative restriction

Focus on Small Business

International markets

Monika had worked and grown her candy business for three years. She sold chocolate and mint candies that were very popular in her store and with her Internet customers. She recently visited friends in Vienna, Austria, and took them some of her candy as a gift. They loved her candy as did their friends. Monika began to wonder if there would be a market for her candy in other countries. She went to her friend Lazlo for advice because he has experience selling antiques in the United States and other countries.

Work as a Team What advice do you think Lazlo might give Monika? What things should Monika research before deciding to sell her candy outside of the United States?



© PhotoDisc/Getty Images

Selling globally can be a way to grow your business.

Exports and Imports

The global marketplace has dramatically changed the way businesses operate. It has made business more competitive, and it has opened new opportunities for companies, including small entrepreneurial businesses. As the global marketplace continues to expand, entrepreneurs can take advantage of even more opportunities.

International trade is one way you can become part of the global marketplace. This means you would export or import the products or services you sell or use in your business.

Exporting

Products and services that are produced in one country and sent to another country to be sold are **exports**. The United States exports agricultural products, automobiles, machinery, computers, and more. These products are shipped to countries all over the world.

DIRECT EXPORTING You can find buyers or distributors in foreign markets and ship your products to them. This is called *direct exporting*. For direct exporting, you may need to hire salespeople who live in or travel to the foreign countries.

Tiffany Wilson owns a mid-sized printing company. Last year, Tiffany decided to expand her business internationally. She hired a Dutch sales representative, Mieta Van Praag, to market her business in Europe. Mieta calls on customers in the Netherlands and France.

INDIRECT EXPORTING It can be difficult to make contacts with buyers in other countries. Some businesses use *commissioned agents* who act as brokers to find foreign buyers for products and services. Exporting through commissioned agents is *indirect exporting*.

SELLING WORLDWIDE THROUGH THE WEB Another way to get involved in exporting is through the World Wide Web. Businesses translate and modify their web sites to appeal to foreign customers. They fill individual orders and ship them directly to the foreign customer's address.

Shahid Mahmoud's business manufactures puzzles. He recently began promoting his products abroad over the World Wide Web because research showed that Japanese buyers like puzzles. To target that market, he created an e-commerce web site written in Japanese.

Importing

Products and services that are brought in from another country to be sold are **imports**. The United States imports many products such as automobiles from Europe, Japan, and Korea and oil from the Middle East.

Entrepreneurs may decide to import products to sell or to use in the production of their product. Price and quality are usually factors in their decision to import. Consumers like low prices and demand high quality.

James Sutton owns a business that makes African-style clothing. He imports all of his fabrics from West Africa because of their unique colors, designs, and textures. James's customers appreciate his attention to detail in creating authentic African clothing.



© PhotoDisc/Getty Images

Why might direct exporting be more difficult than indirect exporting?

Checkpoint

Why do entrepreneurs choose to participate in the global marketplace by exporting and importing products and services?



Is International Business Right for You?

Not every business can succeed internationally. You need to consider the pros and cons of competing globally. Then, you must determine whether there is a market for your business in other countries and write an international business plan.

Reasons for Competing Globally

As discussed in Chapter 12, there are many risks associated with competing in the global marketplace. There are also many benefits that international business can provide, including increased profits. There are at least three good reasons to expand into other countries:


1. **Increased sales** You will attract new buyers and broaden your customer base. You may also import unique products that local customers can buy.
2. **Reduced costs** Manufacturers in other countries can produce goods less expensively because of low labor costs or availability of raw materials. This can mean a savings for you in the form of a lower price.
3. **Decreased dependence on current markets and suppliers** If economic conditions in the United States suddenly worsen, foreign markets and suppliers might help keep your profits high. Selling products and services abroad can also help you stabilize seasonal market fluctuations.

Analyze the Market

Analyzing whether there is an international market for your product will be very similar to how you analyzed your current target market and target customers. But in addition to the kind of analysis you learned about in Chapter 4, you will need to consider other factors, including political, economic, social, and cultural issues. Additional taxes and regulations are also things to research and consider.

Various resources are available that can help you learn about doing business abroad.

- Trade fairs and seminars sponsored by the U.S. Department of Commerce
- Dun and Bradstreet's *Exporter's Encyclopedia*
- Trade statistics from the Bureau of the Census and the Small Business Administration
- Federal or state government market studies on your industry's potential abroad


BE YOUR OWN BOSS

You manufacture toys for small children. You have found a manufacturer overseas who will make your toys for less than half of what you pay to have them manufactured in the United States. You are considering using the overseas manufacturer, but you want to be sure it uses quality materials, provides safe working conditions, and does not use child labor. Use the six-step problem-solving model to determine if you will use the overseas manufacturer.



© PhotoDisc/Getty Images

Why should business owners analyze the foreign markets in which they want to do business?

Mark Milowski owns a business that processes payroll records. He recently met with several Hong Kong business owners who wanted Mark's company to handle their payrolls. Mark liked the idea of expanding globally, but he had many questions. He contacted the Department of Commerce to get information on doing business in Hong Kong. In addition, he referenced the *Exporter's Encyclopedia* to learn about the regulations he would face.

Write an International Business Plan

An international business plan is an extension of your business plan. It sets forth your goals for international expansion and defines the strategies for achieving those goals. Your plan should indicate the following:

- Why you want to expand your business into the global marketplace
- Which foreign markets you plan to enter and why
- What revenues your venture is expected to earn
- How you plan to finance your global expansion
- What costs (travel, shipping, marketing) you expect to have
- How you plan to market and sell your products or services abroad
- How you plan to deliver your products or services to foreign markets
- What legal requirements you will need to meet to sell your products or services abroad

Checkpoint

What are some sources of information that can help you learn about doing business abroad?



Government Regulation of International Trade

Some governments establish **trade barriers**, which are methods for keeping foreign businesses from competing with domestic producers. Quotas, tariffs, and qualitative restrictions are trade barriers. You will need to research the existing trade barriers that may affect your global expansion.

Quotas

A **quota** is a limit on the amount of a product that can be imported into a country over a particular period of time. Japan places quotas on the number of foreign automobiles that can be imported. These quotas protect Japanese car makers from losing business to foreign competitors.

Tariffs

A **tariff** is a tax on imports. Governments use tariffs to protect domestic manufacturers of products that compete with imports. The United States places a tariff on imported sugar. Foreign companies that sell their sugar in the United States must pay a tax. This makes their product more expensive and less competitive with sugar produced in the United States.

Qualitative Restrictions

A **qualitative restriction** is a standard of quality an imported product must meet before it can be sold. A qualitative restriction can keep foreign businesses from competing with domestic producers. It is also used to protect consumers. For example, the United States insists that all meat sold in this country meet certain sanitary regulations and that imported toys meet U.S. safety requirements.



© Digital Vision/Getty Images

What problems might occur if imported products did not have to meet qualitative restrictions?

The North American Free Trade Agreement

Implementation of the North American Free Trade Agreement (NAFTA) began January 1, 1994. This agreement removed most barriers to trade and investment among the United States, Mexico, and Canada. This means that U.S. businesses can sell their products and services in Canada and Mexico just as they would in the United States. It also means that the United States imposes no quotas or tariffs on imports from Canada and Mexico. NAFTA makes it much easier to export and import products and services within North America.

Government Assistance to Companies Operating Abroad

Dozens of different government agencies are available to answer your questions about doing business overseas. They include the following:

- **The Office of International Trade of the Small Business Administration** The mission of this agency is to enhance the ability of small businesses to compete in the global marketplace. It works to facilitate access to capital to support international trade and to ensure that the interests of small businesses are considered and reflected in trade negotiations.

Famous Entrepreneur

Johnny Pag

The Johnny Pag Company manufactures a motorcycle line in China that is affordable for the average American. Johnny Pag has designed and built custom motorcycles for the past 30 years in Corona, California. He is well respected among his peers and has a keen eye for quality and style. He was commissioned by his son JR, the owner of Johnny Pag, to head up the design and building of the complete JohnnyPag.com line of motorcycles. He went overseas, taking his own designs, molds, and tools. He then guided the Wenzhou, Chinese welders and assemblers on how to build the Spyder bike line on their equipment and machines. The Chinese have built top-quality motorcycles for the European market for the past 25 years. By manufacturing the bikes in China, the retail cost is one-third the cost of motorcycles manufactured in the United States due to labor rates and regulations.

In 2006, Johnny Pag entered into a joint partnership with his Chinese contacts. State-of-the-art equipment was installed in the new Chinese production facility. Quality standards were established to create a bike that gives the customer personal pride as well as safety assurance. With the Johnny Pag name on each motorcycle, the company stands by its product and places an emphasis on customer service.

Think Critically

Manufacturing costs are lower in Asian countries than in the United States. Some people view this as taking jobs away from Americans. Others see it as a way of making a better product that is more affordable for Americans. What do you think about outsourcing manufacturing overseas?



How did the Johnny Pag Company grow its business?

© Courtesy of Johnny Pag Motorcycles

- **The International Trade Administration** This bureau of the U.S. Department of Commerce promotes trading and investing, strengthens industry competitiveness, and ensures fair trade.
- **Bureau of Industry and Security** The Bureau of Industry and Security is another bureau of the U.S. Department of Commerce. Its mission is to advance U.S. national security, foreign policy, and economic objectives. It works to ensure an effective export control and treaty compliance system and promotes continued U.S. strategic technology leadership.

In addition to these agencies, the federal government offers many programs that help U.S. businesses operate in foreign markets. The programs include export counseling, export financing, and technical assistance.

Checkpoint

Name three methods that governments use to regulate international trade.

13.3 Assessment

THINK ABOUT IT

1. As an entrepreneur, what do you think are the pros of competing globally? What do you think are the cons of competing globally?
2. Do you think it is in our country's best interest to have U.S. companies engage in international trade? Why or why not?
3. What do you think would happen to the U.S. economy if there were no quotas on imported goods?

MAKE ACADEMIC CONNECTIONS

4. **MATH** A government in an Asian country applies a 20 percent tariff to all electronic goods imported to the country. If it collects \$24 million in tariffs for these goods, what was their total value?
5. **RESEARCH** Research the North American Free Trade Agreement (NAFTA) and write a one-page report on what you learn. State your opinion on whether or not NAFTA is beneficial to the United States.



TEAMWORK

You own a clothing boutique and have recently expanded into catalog sales to sell your products abroad. Select a country in which you want to sell. Working with team members, determine what method of exporting you will use. Discuss some of the government regulations that will affect your business. Think about how you might obtain further information about these regulations. Share your team's ideas with the rest of the class.



Sharpen Your Entrepreneurial Skills

Time Management

You have learned that an entrepreneur has many responsibilities. You are probably wondering how you can fit everything into one day! Good time management skills are essential to the success of your business.

In learning to manage your time, the first thing you should do is establish a plan. A plan forces you to think ahead, which helps you manage your time more effectively. A plan should list all of the routine tasks of your business as well as those tasks related to growing your business.

After creating a plan, you should prepare a “to do” list containing all of the tasks outlined in your plan. Prioritize the tasks from high priority to low priority. Assign due dates to each task. Review your list at the beginning of each day and again at the end of the day. Cross off tasks that have been completed, add new tasks that have come up, and reprioritize your list of tasks as necessary. Do not be afraid to ask for help as you grow your business. You may get to the point where you will not be able to do it all. There may also be tasks that you do not have the expertise to complete. To make effective use of your time, look for others who you can contract with or hire to perform these tasks. For example, you may contract with an accountant to do your financial recordkeeping and reporting.

Remember to allow for personal time. Take breaks occasionally. If you are working too much and overly stressed, you will not be an effective leader. Take time out for physical activities and to spend time with friends and family.

TRY IT OUT

Before you can schedule your time, you need to understand how you use your time. Using the Activity CD, open the activity “Time Log.” Print out a copy and complete the activity log by keeping track of your daily activities over a certain period of time.



© PhotoDisc/Getty Images



Chapter 13 | Assessment

SUMMARY

13.1 Growth Strategies

1. Determining when to expand your business depends on two main factors: the condition of your business and the economic conditions in the market in which your business competes.
2. Businesses that experience uncontrolled growth may find themselves overextended with inadequate resources to support the new level of business. You will want to create a plan for growth.
3. Growth strategies include market penetration, geographic expansion, and market development.
4. The stages of the product life cycle include introduction, growth, maturity, and decline. Steps in new product development include idea development, idea screening, strategy development, financial analysis, product development and testing, and product marketing.

13.2 Ethical and Social Issues

5. Ethics is the study of moral choices and values.
6. Entrepreneurs should create a code of ethics to establish appropriate behavior in the workplace.
7. An entrepreneur has social responsibilities involving customers, suppliers, creditors and investors, and the community.
8. Ways to meet your business's environmental responsibilities include to conserve resources, reduce waste by recycling, dispose of waste responsibly, and sell environmentally friendly products and services.

13.3 Global Trends and Opportunities

9. Entrepreneurs participate in the global marketplace through direct and indirect exporting, importing, and selling through the Web.
10. To determine if international business is right for you, consider the pros and cons of competing globally and write an international business plan.
11. Trade regulations that will affect your international business include quotas, tariffs, and qualitative restrictions established by the countries in which you will be doing business.

What do you know now?

Read Ideas in Action on page 361 again. Then answer the questions a second time. How have your responses changed?

VOCABULARY BUILDER

Match each statement with the term that best defines it. Some terms may not be used.

1. The application of the principles of right and wrong to issues that come up in the workplace
2. A strategy for expanding the target market of a business
3. A limit on the amount of a product that can be imported into a country over a particular period of time
4. Products and services that are brought in from another country to be sold
5. The study of moral choices and values
6. Increasing market share for a product or service within a given market in a given area
7. Products and services that are produced in one country and sent to another country to be sold
8. A set of standards or rules that outlines the ethical behavior demanded by an individual, a business, or a culture
9. Methods for keeping foreign businesses from competing with domestic producers
10. The stages a product goes through from the time it is introduced to when it is no longer sold
11. A tax on imports
12. A standard of quality an imported product must meet before it can be sold

- a. business ethics
- b. code of ethics
- c. ethics
- d. exports
- e. imports
- f. market development
- g. market penetration
- h. product life cycle
- i. prototype
- j. qualitative restriction
- k. quota
- l. tariff
- m. trade barriers

REVIEW YOUR KNOWLEDGE

13. **True or False?** The condition of your business and the economic conditions of the market in which you compete help determine when you should expand your business.
14. Which of the following is *not* a factor to consider when analyzing the economic climate that controls your business?
 - a. condition of national economy
 - b. new competition
 - c. demographic changes
 - d. prices you charge
15. A prototype of a product is created during which stage of new product development?
 - a. idea screening
 - b. strategy development
 - c. product development and testing
 - d. product marketing
16. **True or False?** During the introduction stage of a product's life cycle, people are familiar with the product and what it can do for them.
17. Increasing your advertising and improving your customer service are examples of growing your business through
 - a. market penetration
 - b. geographic expansion
 - c. market development
 - d. none of the above

18. **True or False?** Culture has no effect on the ethics of an individual.
19. **True or False?** Ethical behavior is good for business because it gains the trust of customers.
20. **True or False?** For a business to successfully diversify, it needs to develop products that are unrelated to the products it already sells.
21. The North American Free Trade Agreement (NAFTA) removed most barriers to trade and investment among the United States and
 - a. China and Japan
 - b. Mexico and Cuba
 - c. Mexico and Canada
 - d. Canada and Korea
22. Which of the following is *not* an example of fulfilling environmental responsibilities?
 - a. using solar energy to power your heating and cooling systems
 - b. disposing of paper used by your business in the dumpster
 - c. selling a laundry detergent with stain-removing enzymes that do not harm water ecosystems
 - d. following federal guidelines for disposing of hazardous waste
23. **True or False?** Global competition has had no impact on the way businesses operate.
24. Selling in foreign markets through commissioned agents is known as ____.
25. **True or False?** Any business can have success competing internationally.
26. As an entrepreneur, you have a personal responsibility to all of the following *except*
 - a. your community
 - b. your customers
 - c. your creditors and investors
 - d. your competitors

APPLY WHAT YOU LEARNED

27. You publish a cooking magazine that is circulated in your local metro area. How can you expand your business? What growth strategy will you employ? Write a plan for growth that includes setting and achieving measurable objectives, hiring managers, financing the expansion, and obtaining resources for expansion.
28. You have opened a delicatessen in your town. What are some of the responsibilities you have to your customers? In what ways can your business benefit the community? How do you think fulfilling these responsibilities will help your business?

MAKE ACADEMIC CONNECTIONS

29. **COMMUNICATION** Use the Internet, newspapers, and magazines to find examples of two companies that are environmentally responsible and one company that has violated environmental laws. Give a presentation to the class that details the companies' actions and their impact on society.
30. **MATH** You have a business selling concrete to contractors. One of your suppliers in South America has quoted a price of \$4.00 per 50-pound bag. Your U.S. supplier is charging \$4.50 per 50-pound bag. Both suppliers have agreed to cover shipping costs, but the foreign

company must pay a 12.5 percent tariff on each bag shipped and will pass that cost on to you. Which supplier will you buy from and why?

31. **RESEARCH** Choose a business that has recently introduced a new product to the market. Research the company and find out what other products it had on the market before the introduction of the new product. Was the new product introduced to replace an existing product or to capture a new market?

WHAT WOULD YOU DO?



You are an independent contractor hired by the state to inspect paving work done on a highway. The paving company had to complete the job on time or pay a fine to the state. In order to meet the deadline, the paving company did not follow all of the specifications in the contract. The president of the company has asked you to approve the job in exchange for a large sum of money. What are the ethical issues you face? What do you think would be the best way to resolve the issue? Who will be affected by your decisions?

BUILD YOUR Business Plan *Project*

This activity will help you think about growing your business, conducting business ethically, and expanding your business globally. You will also finalize the business plan that you have been working on throughout the book.

1. What will indicate that you are ready to expand your business? Give specific examples, such as your sales growing by 20 percent or your business outgrowing its current location.
2. What effect can the present economy have on your business? Write a growth plan that includes strategies for attaining measurable objectives, hiring managers, financing expansion, and obtaining resources for expansion.
3. Write a code of ethics for your business that includes company policies and procedures for dealing with particular situations. What are some situations that are specific to your type of business that may pose an ethical dilemma?
4. Write an environmental policy for your business. What are some of the actions your business will take to protect the environment? Are these actions required by law? If not, why will you incorporate them into your policy?
5. What global opportunities exist for your business? Determine the best country in which your business could expand. List the specific benefits and risks of global expansion for your business.
6. Put it all together! Now that you have researched the different aspects of starting your own business, you are ready to use the information you have gathered in the Build Your Business Plan Project to compile your business plan. Using the Activity CD, open the activity "Business Plan Template" to help you complete your final business plan.



Planning a Career in Transportation



"My mom's husband has a job that requires travel to a lot of big cities. He often arranges to have a limousine pick him up at the airport and take him to his destination. It saves him a great deal of time to have the limo driver waiting for him when he arrives. At his level in the organization, it makes sense financially to pay a bit more for his transportation and get him to his meetings as quickly as possible."

How do people traveling to various cities get from the airport to their destination easily? How do people who have a physical disability that prohibits them from driving get to their appointments?

Chauffeurs are individuals who provide transportation to clients on a prearranged basis. Chauffeurs may be employed by an individual, family or business. Some chauffeurs may have multiple duties for an employer. Additional duties might include personal security, household help, or administrative assistance.

EMPLOYMENT OUTLOOK

- Faster than average growth is anticipated.
- About a quarter of chauffeurs are self-employed.
- Large, thriving cities will offer the best opportunities.

JOB TITLES

- Luxury Vehicle Chauffeur
- Driver/Chauffeur
- Chauffeur/Houseman
- Chauffeur/Professional Driver
- Chauffeur/Executive Protection
- Personal Chauffeur

NEEDED SKILLS

- A high school diploma is preferred.

- A good driving record is necessary.
- In addition to a regular driver's license, a chauffeur's license is required. Licensing requirements vary by state.
- Good interpersonal skills to handle a variety of customer personalities are important.
- Familiarity with the local terrain and good map-reading skills are helpful.
- The minimum age requirement is often 21.

What's it like to work in Transportation?

Pedro has been leasing his limousine for two years. Paying a monthly fee to the limousine company entitles Pedro to full use of the vehicle, even when he isn't working. His monthly payment also covers routine vehicle maintenance and insurance fees. Pedro is saving money for a down payment on his own limousine.

Tonight Pedro is scheduled to drive a bride and groom from their wedding ceremony to their reception. After the reception, he will drive them to their hotel.

For the first three days of next week, Pedro is scheduled to provide transportation for a repeat client. The client, an executive who visits Pedro's city each month, often books Pedro's time for a series of days. When Pedro isn't driving the client to a destination, he often runs errands for the client. At the end of next week, Pedro is scheduled to drive a visually impaired client on a variety of errands.

What about you? Would you enjoy driving an array of clients on a variety of trips throughout your city?



SMALL BUSINESS MANAGEMENT TEAM EVENT

The Small Business Management Team Event requires participants to provide advice to a startup business.

Three early-retiree teachers want to start their own business, Head of the Class, that will provide training to new teachers. They have noticed that the number of teacher education programs has declined, and many new teachers are not fully equipped to successfully handle classroom management. The business will work directly with school districts and universities that have reduced teacher-training programs. The three retired teachers have set up an appointment to meet with the Small Business Forum to seek assistance and financing in opening this business operation. The three entrepreneurs have \$10,000 each in savings that they plan to use for their startup business.

Your team of two to four members will serve as consultants to the three entrepreneurs. You will provide them with information that they need for their presentation to the Small Business Forum. You must be aware of the location, competition, and the budget needed to successfully operate this business. You will help the entrepreneurs determine what makes their business unique and give them ideas to convince the Small Business Forum to provide financial assistance. You must also suggest ideas for growing the business.

Prepare an oral presentation that addresses the questions that follow. You will have ten minutes to make your presentation and an additional ten minutes to answer the judge's questions.

PERFORMANCE INDICATORS EVALUATED

- Evaluate and delegate responsibilities needed to perform required tasks.
- Demonstrate teamwork skills needed to function in a business setting.
- Demonstrate self-esteem, self- and team-management, and integrity.
- Demonstrate a working knowledge of business management concepts.
- Demonstrate critical thinking skills to make decisions and solve problems.
- Demonstrate a working knowledge of entrepreneurial concepts.

Go to the BPA web site for more detailed information.

Think Critically

1. How can the proposed business save school districts money?
2. What statistics can be used to prove the need for this business?
3. What is the potential growth for this business?
4. Why should school districts use the services offered by this business?

www.bpa.org

Glossary



A

Account An accounting record that provides financial detail for a particular business item, such as for cash, sales, rent, and utilities

Advertising A paid form of communication sent out by a business about a product or service; it keeps a product or service in the public's eye by creating a sense of awareness and helps convey a positive image

Advertising fees Fees paid to a franchise company to support television, magazine, or other advertising of the franchise as a whole

Aptitude The ability to learn a particular kind of job

Authoritative management Management style in which the manager is directive and controlling

B

Balance sheet A financial statement that lists what a business owns, what it owes, and how much it is worth at a particular point in time

Benefits Employment rewards for service in addition to salary; rewards may include paid leave, insurance, and a pension plan

Board of directors Group of people who meet several times a year to make important decisions affecting the company

Bonus Financial rewards made in addition to a regular wage or salary that usually hinge on reaching an established goal

Bounced check Check that is returned to a business by the bank because the customer's checking account has insufficient funds to cover the check amount

Brainstorming A creative problem-solving technique that involves generating a large number of fresh ideas

Branding The name, symbol, or design used to identify a product

Business ethics Application of the principles of right and wrong to issues that come up in the workplace

Business plan A written document that describes all the steps necessary for opening and operating a successful business

C

Capitalism The private ownership of resources by individuals rather than by the government

Cash budget Show the projections of cash coming in and going out of a business

Cash flow statement An accounting report that describes the way cash flows into and out of a business over a period of time

Channels of distribution Routes that products and services take from the time they are produced to the time they are consumed

Check register Booklet in which an account holder records the dates and amounts of the checks as well as the names of people or businesses to whom he or she has written the checks

Code of ethics A set of standards or rules that outline the ethical behavior demanded by an individual, business, or culture

Collateral Property that a borrower forfeits to the bank providing the loan if he or she defaults on the loan

Commission A percentage of a sale paid to a salesperson

Competition-based pricing Pricing that is determined by considering what competitors charge

Competitive analysis Identifying and examining the characteristics of a competing firm

Consumer credit Offered when a retail business allows its customers to buy merchandise now and pay for it later

Contract Legally binding agreement between two or more persons or parties

Controllable risk Risk that can be reduced or possibly even avoided by actions the insured takes

Copyright Form of intellectual property law that protects original works of authorship, including literary, dramatic, musical, and artistic works

Corporation Business that has the legal rights of a person but is independent of its owners

Cost-based pricing Pricing determined by using the wholesale cost of an item as the basis for the price charged

Cover letter Letter that introduces and explains an accompanying document or set of documents

Customer profile Description of the characteristics of the person or company that is likely to purchase a product or service

D

Debt capital Money loaned to a business with the understanding that the money will be repaid, usually with interest

Debt-to-equity ratio The relation between the dollars borrowed and the dollars invested in a business

Delegate To allow other people to share workloads and responsibilities

Demand Individual's need or desire for a product or service at a given price

Demand-based pricing Pricing that is determined by how much customers are willing to pay for a product or service

Democratic management Management style in which employees are involved in decision making and the manager provides less direction

Demographics Data that describe a group of people in terms of their age, marital status, family size, ethnicity, gender, profession, education, and income

Direct channel Moves the product directly from the manufacturer to the consumer

Direct competition Comes from a business that makes most of its market as other businesses

Discount pricing Offers customers a reduced price encouraging them to buy

Distribution An important component of the marketing mix that involves the locations and methods used to make products available to customers

Dividends distributions of corporate profits to the shareholders

E

Economic decision making The process of choosing which needs and wants, among several, will be

satisfied using the resources on hand

Economic resources Means through which goods and services are produced

Emotional buying decisions

Based on the desire to have a specific product or service; feelings, beliefs, and attitudes influence a consumer's buying decisions, who often spends little thought or time in making the decision

Employees People who work for someone else

Enterprise zones Areas that suffer from lack of employment opportunities

Entrepreneurs People who own, operate, and take the risk of a business venture

Entrepreneurship Process of running a business of one's own

Equilibrium price and quantity Point at which the supply and demand curves meet

Equity capital Money invested in a business in return for a share in the profits of the business

Ethics The study of moral choices and values; involves choosing between right and wrong

Executive summary A short restatement of the report portion of a business plan

Exports Products and services that are produced in one country and sent to another country to be sold

F

Federal Employees' Compensation Act (FECA) Law that provides benefits to employees who have suffered work-related injuries or occupational diseases; benefits include payment of medical expenses, compensation for lost wages, and payment of benefits to dependents of employees who die from work-related injuries or diseases

Fixed costs Costs that must be paid regardless of how much of a good or service is produced

Focus group In-depth interview with a group of target customers who provide valuable ideas on products or services for the same good or service

Franchise Legal agreement that gives an individual the right to market a company's products or services in a particular area

Freelancers People who provide specialty services to businesses on an hourly basis or by the job

G

Geographic data Data that helps a business determine where its potential customers live and how far they will travel to visit the business

Gross lease Occurs when the tenant pays rent each month for the space occupied, and the landlord covers all property expenses for that space

Gross sales The dollar amount of all sales

I

Ideas Thoughts or concepts that come from creative thinking

Imports Products and services that are brought from one country into another country to be sold

Income statement Shows the business's revenues and expenses incurred over a period of time and the resulting profit or loss

Indirect channel Distribution channel that uses intermediaries to move products between the manufacturer and the consumer, such as agents and wholesalers

Indirect competition Comes from a business that makes only a small amount of money selling the same or similar products and services to the same market as other businesses

Industrial park Section of land that is zoned for industrial businesses only; usually located where space is less expensive, away from housing developments and downtown areas

Initial franchise fee Amount the local franchise owner pays in return for the right to run the franchise; fee can run anywhere from a few thousand to a few hundred thousand dollars. It is usually nonrefundable.

Intellectual property The original, creative work of an artist or inventor and may include such things as songs, novels, artistic designs, and inventions.

Interns Students who will work for little or no pay in order to gain experience in a particular field.

Inventory The merchandise a business sells to its customers.

J

Job analysis Process of determining the tasks and sequence of tasks necessary to perform a job.

Job description Written statement listing the tasks and responsibilities of a position; also covers to whom the position reports, educational and professional experience required, and salary range.

Journals Accounting records of the transactions you make; there are five different journals that businesses use to record their transactions.

L

Landlord Person who owns and rents out buildings or space.

M

Management Process of achieving goals by establishing operating procedures that make effective use of people and other resources.

Manager Person responsible for planning, organizing, staffing, implementing, and controlling the operations of a business.

Marginal benefit Measures the advantages of producing one additional unit of a good or service.

Marginal cost Measures the disadvantages of producing one additional unit of a good or service.

Market development Strategy for expanding the target market of a business.

Marketing All of the processes used to determine and satisfy the needs of customers and the company.

Marketing concept Uses the needs of customers as the primary focus during the planning, production, distribution, and promotion of a product or service.

Marketing mix Blending of the product, price, distribution, and promotion used to reach a target market.

Marketing plan Defines market, identifies customers and competitors, outlines a strategy for attracting and keeping customers, and identifies and anticipates change.

Marketing strategy Plan that identifies how marketing goals will be achieved; a startup marketing plan should address: product introduction or innovation, pricing, distribution, promotion, projected profitability, and sales or market share.

Market penetration Increasing market share for a product or service within a given market in a given area.

Market research System for collecting, recording, and analyzing information about customers, competitors, goods, and services.

Market segments Groups of customers within a large market who share common characteristics.

Market share Business's percentage of the total sales generated by all companies in the same market.

N

Needs Those things that a person must have in order to survive.

Net lease Occurs when the landlord pays building insurance, and the tenant pays rent, taxes, and any other expenses.

Net sales The dollar amount of all sales with any returns subtracted.

Net worth Difference in what is owned, called *assets*, and what is owed, called *liabilities*.

O

Operations manual Contains all of the rules, policies, and procedures that a business should follow in order to function effectively.

Opportunities Possibilities that arise from existing conditions.

Opportunity cost Value of the next-best alternative.

Organizational chart Shows who reports to whom in the company, or the chain of command.

Organizational structure Plan that shows how the various jobs in a company relate to one another; often represented in a chart and indicates the working relationships within the business.

P

Partnership Business owned by two or more people.

Patent The grant of a property right to an inventor to exclude others from making, using, or selling his or her invention; intent of a patent is to give the developer of a new product time to recover the development costs without having to worry about competition.

Payroll List of people who receive salary or wage payments from a business.

Percentage lease Tenant pays a base rent each month, and the landlord also receives a percentage of the tenant's revenue each month.

Performance evaluation Management control tool that helps determine whether the objectives for a particular job are being met.

Periodic inventory method Involves taking a physical count of your merchandise at regular intervals, such as weekly or monthly.

Perpetual inventory Method keeps track of inventory levels on a daily basis; can make a business more efficient and ensure that it never runs out of stock.

Personal selling Direct communication between a prospective buyer and a sales representative in which the sales representative attempts to influence the prospective buyer in a purchase situation

Physical distribution Includes transportation, storage, handling, and packaging of products within a channel of distribution

Point-of-sale system Cash registers with a software system that updates inventory records as each sale happens; bar-code scanners and credit card authorization systems can be integrated into the POS system

Positioning Creating an image for a product in the customer's mind

Premium Payment that is made to an insurance company to cover the cost of insurance; price paid to cover a specified risk for a specific period of time

Press release Written statement meant to inform the media of an event or product

Primary data Information collected or the very first time to fit a specific purpose

Pro forma financial statement Financial statement based on projected revenues and expenses

Product life cycle Stages a product goes through from the time it is introduced to when it is no longer sold; a product goes through four stages in its life cycle: introduction, growth, maturity, and decline

Product mix Different products and services a business sells

Profit sharing Compensation arrangement in which employees are paid a portion of the company's profits

Profit Difference between the revenues taken in by a business and the costs of operating the business

Prototype full-scale model of a new product

Psychographics Data that describe a group of people in terms of their tastes, opinions, personality traits, and lifestyle habits

Psychological pricing Pricing method based on the belief that certain prices have an impact on how customers perceive a product

Public relations Act of establishing a favorable relationship with customers and the general public

Publicity Nonpaid form of communication that calls attention to a business or event through media coverage

Pure risk Insurable risk that is faced by a large number of people and the amount of the loss can be predicted; presents the chance of loss but no opportunity for gain

Q

Qualitative restriction Standard of quality an imported product must meet before it can be sold; it can keep foreign businesses from competing with domestic producers and protect consumers from dangerous foreign products

Quota Limit on the amount of a product that can be imported into a country over a particular period of time

Quote An estimate for how much will be paid for merchandise or service

R

Rational buying decisions

Based on the logical reasoning of customers

Rebate Refund offered to people who purchase a product

Recruit To look for people to hire and attract them to the business

Reorder point Predetermined level of inventory that signals when new stock should be ordered

Return on investment (ROI)

Amount earned as a result of the investment, usually expressed as a percentage

Risk assessment Involves looking at all aspects of a business and determining the risks it faces

Risk management Involves taking action to prevent or reduce the possibility of loss to a business

Risk Possibility of some kind of loss; categorized as human risk, natural risk, and economic risk

Royalty fees Weekly or monthly payments made by the local owner to the franchise company; these payments usually are a percentage of a franchise's income

S

Salary Amount paid for a job position stated on an annual basis

Sales promotion Incentive offered to customers in order to increase sales; examples include contests, free samples, rebates, coupons, special events, gift certificates, and frequent-buyer reward programs

Scarcity Occurs when people's needs and wants are unlimited and the resources to produce the goods and services to meet those needs and wants are limited

Secondary data Data found in already-published sources

Self-assessment Evaluation of your strengths and weaknesses

Service Corps of Retired Executives (SCORE) Group made up of more than 10,500 retired executives who volunteer their time to provide entrepreneurs with real-world advice and know-how

Share of stock Unit of ownership in a corporation

Shoplifting Act of knowingly taking items from a business without paying

Small Business Administration (SBA) Independent agency of the federal government that was created to help Americans start, build, and grow businesses

Small Business Development Centers (SBDC) Provides management assistance to current and prospective small business owners

Sole proprietorship Business that is owned exclusively by one person; enables one person to be in control of all aspects of the business

Speculative risk Risk which offers the insured the chance to gain as well as lose from the event or activity

Staffing Involves determining the number of employees a company needs and defining a process for hiring them

Startup costs Costs associated with beginning a business including the costs of renting a facility, equipping the outlet, and purchasing inventory

Statement of purpose Brief explanation of why the writer of a business plan is asking for a loan and an explanation of what he or she plans to do with the money

Stock card Paper inventory record for a single item

Stock turnover rate Rate at which the inventory of a product is sold and replaced with new inventory

Supply How much of a good or service a producer is willing to produce at different prices

Survey List of questions to ask customers to find out demographic and psychographic information; can be conducted by mail, over the phone, on the Internet, or in person

T

Target market Includes the individuals or companies that are interested in a particular product or service and are willing and able to pay for it

Tariff Tax on imports that governments use to protect domestic manufacturers of products that compete with imports

Tenant Person who pays rent to occupy space owned by someone else

Total product Product characteristics that will satisfy customer needs, including such things as color, size, quality, hours, warranties, delivery, and installation

Trade area Area from which a business expects to attract customers

Trade associations Organizations made up of professionals in a specific industry

Trade barriers Methods for keeping foreign businesses from competing with domestic producers

Trade credit Offered when one business allows another business to buy now and pay later

Trademark Name, symbol, or special mark used to identify a business or brand of product

Trade shows Special meetings where companies of the same or

related industry display their products, can also be beneficial

Transaction Any business activity that changes assets, liabilities, or net worth

U

Uncontrollable risk Risk on which actions have no effect, such as the weather

Use-based data Data that helps a business determine how often potential customers use a particular service

V

Variable costs Costs that go up and down depending on the quantity of the good or service produced

Vendors Companies that sell products and services to businesses

Venture capitalists Individuals or companies that make a profit investing in startup companies

W

Wages Payments for labor or services that are made on an hourly, daily, or per-unit basis

Wants Those things that a person thinks he or she must have in order to be satisfied



Index

A

- Accident insurance, 312
- Account, 254–255
- Accountant, 180
- Accounting. *See* Financial statements
- Accounting equation, 250
- Accounts payable
 - as current liabilities, 251
 - defined, 251
 - ledger, 255
- Accounts receivable
 - as current assets, 251
 - defined, 251
 - ledger, 255
- Accounts receivable financing, 242–243
- A-Corp, 94
- ADA. *See* Americans with Disabilities Act (ADA)
- Adizes, Ichak, 272
- Advertising
 - classified, 303
 - defined, 154–155
 - direct-mail, 159
 - dollars spent on, 155
 - fees (franchise), 181
 - in-store, 305
 - magazine, 159–160
 - message choice, 155
 - newspaper, 158
 - online, 155–156
 - outdoor, 160
 - promotion budget, 160
 - radio, 157–158
 - telephone directory, 158, 225
 - television, 156–157
 - transit, 160
 - want ads, 303

See also Promotion; Publicity
- Advertising Age*, 157
- Age Discrimination in Employment Act, 313
- Agents, as intermediaries, 149
- Aging tables, 255
- Agreement, 200
- Agricultural businesses, 5
- Allowance for uncollectible accounts, 252
- Alps Lawn Company, 361
- Alps Technology, 361
- Alterman, Scott and Greg, 331
- Alternative Apparel, 331
- Americans with Disabilities Act (ADA), 313–314
- American Wholesalers and Distributors Directory, The*, 153
- Annual percentage rate, 198–199
- Antidiscrimination laws, 313–314
- Antitrust legislation, 194–195
- Appearance, of business plan, 77
- Appendix, of business plan, 76
- Apple Computers, 105
- Apply What You Learned, 30, 58, 86, 114, 142, 172, 204, 232, 264, 294, 326, 356, 388
- Aptitude, 14
- Architecture, careers in, 234
- Articles of incorporation, 191–192
- Aslan Computing, 53
- ASPIRA, 63
- Assessment. *See* Self-assessment, for entrepreneurship
- Assets
 - current, 251
 - defined, 250
 - fixed, 251
- Assignment of tasks, in organizing, 271
- Association for Convenience and Petroleum Retailing, 335
- AT&T, 155
- Attorneys. *See* Lawyers
- Audio-video technology, careers in, 328
- Authoritative management style, 272
- Autocratic management style, 272
- Aventis Pharmaceutical Health Care Foundation, 375

B

- Balance, between work and play, 35
- Balance sheet, 250–252
- Banking records, 256–258
- Bank loans, 242–244
- Bank of America Foundation, 375
- Bank reconciliation, 257–258
- Bank statement, 257–258
- Banner ad, 155
- Bar-code scanners, 279
- Barron's* magazine, 181
- Beech, Olive Ann, 3
- Benefits
 - employee, 311–312
 - of products, in selling, 165
- Bentley Entrepreneur Society, 35
- Be Your Own Boss
 - competitive analysis, 107
 - distribution, 150
 - employee taxes, 259
 - functions of business, 47
 - interests, as business idea, 19
 - inventory, 227, 278
 - legal form of business, 192
 - management practices, 316
 - overseas manufacturing, 380
 - psychological pricing, 136
 - robbery, 336
 - SCORE counseling, 80
- Biz Camp, 147, 209
- Blank, Arthur, 7
- BlueStream, 299
- Blue Valley School District (Kansas City, Missouri), 3
- Board of directors, 191
- Bonus, 310
- Borders, Louis, 285
- Borrowing, discussed in business plan, 73
- Bounced checks, 337
- Brainstorming, 24
- Branding, 129
- Breadsmith, 183
- Breakeven analysis, 290
- Breakeven point, 139, 290
- Brin, Sergey, 122
- Budgeting, for promotion, 160
- Build Your Business Plan Project, 31, 59, 87, 115, 143, 173, 205, 233, 265, 295, 327, 357, 389
- Bundling, 136
- Bureau of Industry and Security, 384
- Bureau of the Census, 380
- Business activities in a market economy, 47–48
- Business broker, 179, 180
- Businesses
 - agricultural, 5
 - competition, regulatory promotion of, 194–196
 - consumer-protection laws, 198–199
 - family, 184–185
 - financing for, 240–245
 - franchises, 180–184
 - functions of, 47–48
 - intellectual property and, 196–197
 - legal advice for, 199–200
 - manufacturing, 5, 6
 - mining and extracting, 5
 - number of, in 2005, 6
 - purchasing existing, 178–180
 - purchasing, steps in, 179–180
 - retailing, 5, 6
 - service, 5, 6
 - starting your own, 185–186
 - success or failure, 8–9
 - wholesaling, 5, 6
 - women-owned, 11
 - See also* Competition; International business; Legal forms of business
- Business ethics
 - defined, 371
 - establishing in the workplace, 372–373
 - setting standards, 371–372
 - written code, 372–373
 - See also* Social responsibilities
- Business insurance, 341–342
- Business interruption insurance, 342
- Business letters, 26–27
- Business model, 3
- Business operations, as uninsurable risk, 341
- Business owner's policy (BOP), 341–342
- Business plans
 - advantages over competition, 71
 - appearance of, 77
 - appendix, 76
 - backgrounds and experience of people, 65–66
 - completing, 74–77
 - concluding statement, 73
 - cover letter, 74
 - defined, 64–65
 - detailed description, 70
 - elements, 69–73
 - executive summary, 75–76
 - financial management information, 72–73
 - ideas turned into, 63, 65, 70
 - importance of, 66–68
 - inconsistencies in, 82
 - international, 381
 - introduction, 70–71

- introductory elements, 74–76
- lack of, as reason for loan refusal, 244
- main body, 69–70
- marketing information, 71–72
- mistakes in, 81–82
- objectives of, 65
- operations information, 73
- ownership and legal structure, 70
- parts of, 69–76
- purposes of, 65–66
- research for, 78–81
- skills and experience, 71
- software for, 83
- statement of purpose, 75
- table of contents, 75
- title page, 75
- See also* Build Your Business Plan Project
- Business Professionals of America (BPA).
See WinningEdge
- Business records. *See* Records
- Business risks. *See* Risk
- Business Start-Ups* magazine, 181
- Buying decisions
 - about business space, 218–219
 - rational and emotional, 166
- Buying space, 218–219
- Buzz International Marketing Group, Inc., 177
- C**
- Canada, NAFTA and, 383
- Capacity
 - in a contract, 200
 - in Five Cs of Credit, 63
- Capital, in Five Cs of Credit, 63
- Capital investment, by entrepreneurs, 40–41
- Capitalism, 45
- Capitalization, 35
- Capital resources, 39
- Carrying costs, 280
- Cash budget, 283–284
- Cash disbursements, decreasing, 285
- Cash discounts, 137
- Cash flow
 - cash budget, creating, 283–284
 - cash disbursements, decreasing, 285
 - economic effects on, 248
 - improving, 284–286
 - increasing cash receipts, 284–285
 - managing, 283–286
 - positive or negative, 248
- Cash flow statement, 287
 - defined, 246–247
 - economic effects on cash flow, 248
 - forecasting receipts and disbursements, 247
 - income statement vs., 249
 - preparing, 247–248
- Cash payments journal, 254
- Cash receipts, increasing, 284–285
- Cash receipts journal, 254
- Center for Women’s Business Research, 11
- Chain of command, 302, 333
- Chamber of Commerce, 79, 80, 99, 106, 199
- Change agents, 41
- Channels of distribution
 - defined, 148
 - direct, 149
 - indirect, 149
 - options, 149–150
 - See also* Distribution
- Character, in Five Cs of Credit, 63
- Charisma Cosmetics, 364
- Check, bounced, 337
- Check register, 256
- Child labor laws, 313
- China, economy of, 44
- Choice, 45
- Civil Rights Act of 1964, 313
- Classified advertisements, for job openings, 303
- Clayton Act, 195
- Coaching, of employees, 317
- Codes of ethics
 - defined, 371
 - written, 372–373
- Collateral
 - defined, 242
 - in Five Cs of Credit, 63
 - unsecured loans and, 347
- Collection, of debt, 347, 348
- College placement centers, 304
- Combination pay plan, 311
- Command economy, 43
- Commercial bank loans, 242–244
- Commercial leases, 218–219
- Commercials, 156–157
- Commission, 310
- Commission-based salary, 310
- Commissioned agents, in exporting, 379
- Commission-only pay plan, 310
- Commitment, 12
- Communication, 12, 35
- Communication skills, in problem-solving, 24
- Communism, 44
- Community, responsibilities to, 375–376
- Community shopping centers, 211–212
- Compensation package
 - benefits, 311–312
 - types of pay, 310–311
- Competency, 12

- Competition
 - antitrust legislation and, 194–195
 - customer loyalty and, 109–110
 - defined, 45, 104
 - direct, 105–106
 - global, 350–352, 380
 - ignoring, 82
 - impact of, 104–105
 - increasing market share and, 132–133
 - indirect, 106
 - large retailers as, 107
 - positioning and, 129–130
 - protection of, by government agencies, 195–196
 - regulations that promote, 194–196
 - understanding, 105
- Competition-based pricing, 134–135
- Competitive analysis, 107–108
- Competitive market, 53
- Competitive wages, 311
- Competitor's actions, as uninsurable risk, 340
- Computers, for tracking inventory, 279.
 - See also* Technology
- Concluding statement, of business plan, 73
- Conditions, in Five Cs of Credit, 63
- Conferences, as employee training, 317
- Consideration, 200
- Construction, careers in, 234
- Consumer credit, 346–347
- Consumer demand, as uninsurable risk, 340
- Consumer Guide to Buying a Franchise, A*, 180
- Consumer Product Safety Act of 1972, 198
- Consumer Product Safety Commission, 198
- Consumers
 - awareness of business ethics, 372
 - channels of distribution and, 149–150
 - laws protecting, 198–199
 - See also* Customers
- Contracts
 - defined, 199
 - elements, 200
 - franchise agreements and, 182
 - See also* Partnership agreement
- Controllable risk, 339
- Controlling, in organizing, 273
- Cooperation, 12
- Copyrights, 197
- Corporation
 - advantages, 192
 - defined, 70, 191
 - disadvantages, 191–192
 - limited liability company (LLC), 193
 - reasons for becoming, 192
 - S corporation, 192–193
 - terms used in, 191
- Cost-based pricing, 134
- Cost of goods sold, 250
- Cost per Action (CPA), 156
- Cost per Click (CPC), 156
- Cost per Mil (CPM), 156
- Costs
 - breakeven point and, 139, 290
 - of carrying inventory, 280
 - of doing business, 51–52
 - fixed, 51
 - franchise operating, 181
 - marginal, 51–52
 - marginal benefit and, 51–52
 - opportunity, 46–48
 - startup, 181, 239
 - of stock outages, 281
 - variable, 51
- County Business Patterns*, 18
- Cover letter, for business plan, 74
- Creativity, 11, 12
- Credit
 - consumer, 346–347
 - creditworthiness, 347
 - loans vs., 346–347
 - policies, 347–348
 - risks of, 345–348
 - terms, 347
 - trade, 346
 - types of, 346–347
 - uncollectible accounts, 348
- Credit card authorization systems, 279
- Credit card fraud, 336
- Creditors, responsibilities to, 375
- Credit terms, 286
- Creditworthiness, 347
- Crime insurance, 342–343
- Crocs, Inc., 119
- Cultural diversity, 353
- Culture, ethics and, 370–371
- Current assets, 251
- Current liabilities, 251
- Customer loyalty, 109–110
- Customer profile, 95–96
- Customers
 - calculating rent per, 219
 - decision-making by, 166–167
 - defined, 92
 - determining needs and wants of, 166–167
 - of existing business, 179
 - location and, 210–213, 216–217
 - maintaining loyalty of, 109–110
 - responsibilities to, 374
 - See also* Consumers; Needs; Wants
- Customer service policies, 274

D

DaimlerChrysler, 155
 Data analysis
 in market research, 101
 with spreadsheets, 111
 Data collection, 100–101
 Davis, Phillip, 129
 Debt, personal, avoiding, 53
 Debt capital, 241–245
 Debt-to-equity ratio, 240
 DECA (Delta Epsilon Chi). *See* WinningEdge
 Decision making
 by customers, 166–167
 in different economic systems, 42–44
 See also Economic decision making;
 Problem solving
 Decline stage, of product life cycle, 366
 Delegation of responsibility, 319
 Delivery policies, 274
 Demand
 curve, 50
 defined, 50
 See also Supply and demand
 Demand-based pricing, 134
 Demand elasticity, 50
 Democratic management style, 272
 Demographics, 95
 Dental insurance, 312
 Department of Housing and Urban
 Development (HUD), 244–245
 Department stores, 212
 Depreciation, 252
 Deterioration, of inventory, 280
 Determination, 11
 Develop Your Reading Skills, 5, 37, 65, 93, 121,
 149, 179, 211, 239, 271, 301, 333, 363
 Did You Know?
 advertising dollars, 155
 annual marketing budget, 127
 cost concerns of businesses, 284
 cost of Hurricane Katrina, 339
 family-controlled businesses, 184
 grant-making corporations, 375
 layout design, 220
 minimum wage law, 311
 primary data collection, 99
 scarcity, 46
 SCORE counseling, 79
 Small Business Administration (SBA)
 loans, 245
 women-owned businesses, 11
 Direct channel of distribution, 149
 Direct competition, 105–106
 Direct exporting, 379

Directing management style, 272
 Direct-mail advertising, 159
 Disabled people, protection for, 313–314
 Disaster planning, 333–334
 Disbursements, 247
 Disclosure statement, for franchises, 181–182
 Discount pricing, 137–138
 Discount stores, 212
 Discoveries, 17
 Discrimination, workplace, 313–314
 Dismissal, of employees, 322
 Disney, Walter Elias, 67
 Distribution
 defined, 148
 of goods and services, 150–151
 manufacturing businesses, 151
 retail businesses, 150
 service businesses, 150–151
 Web sites and, 150
 See also Channels of distribution; Physical
 distribution
 Diversification, of products and services, 365
 Diversity, cultural, 353
 Dividends (stock), 191
 DollarDiva Business Plan Competition, 237
 Downen, Aaron, 361
 Downtown location, 210–211
 Drugstores, 212
 Dun and Bradstreet, *Exporter's Encyclopedia*,
 380, 381

E

E-Builder, 91
 Economic conditions, as uninsurable risk, 340
 Economic decision making
 in different economic systems, 42–44
 functions of business and, 47–48
 opportunity cost and, 46–47
 scarcity and, 46
 U.S. economic system and, 45
 Economic Development Administration
 (EDA), 245
 Economic resources
 defined, 38
 factors of production, 39
 goods and services, 38–39
 limited resources, 39–40
 Economic risks, 332
 Economic systems, 42
 command economy, 43
 market economy, 43
 mixed economy, 44
 traditional economy, 43
 U.S., 45, 104

- Economy
 - assessing conditions for growth strategy, 363
 - needs and wants, 36–38
 - scarcity in, 46
 - See also* U.S. economy
- EDA. *See* Economic Development Administration (EDA)
- Eden Body Works, 147
- Edison, Thomas A., 98
- EEOC. *See* Equal Employment Opportunity Commission (EEOC)
- Elastic demand, 50
- E-mail etiquette, 229
- E-marketing, careers in, 144
- Emergency planning, 333–334
- Emotional buying decisions, 166
- Employee compensation
 - benefits, 311–312
 - wages and salary, 310–311
- Employees
 - alternatives to adding, 305–306
 - compensation package, 310–312
 - defined, 5
 - dishonest, 335–336
 - dismissal of, 322
 - entrepreneurs vs., 5
 - evaluating, 320, 321
 - hiring, 307–309
 - listening to, 319
 - managing, 315–322
 - motivation of, 318–319
 - need for, 300–301
 - performance evaluation, 320, 321
 - policy enforcement for, 316–317
 - promotion of, 320
 - recruiting, 303–305
 - regulations that protect, 313–314
 - training, 317–318
- Employee theft, 335–336
- Employment agencies, 304
- Employment outlook, 32, 60, 88, 116, 144, 173, 206, 234, 266, 296, 328, 358, 390
- Empowerment management style, 316
- Enterprise zones, 214
- Entrepreneur* magazine, 181
- Entrepreneurs, 2
 - as change agents, 41
 - defined, 5
 - employees vs., 5
 - present and past, 6–8
 - problem-solving process for, 21–23
 - reasons for becoming, 5
 - role of, in the U.S. economy, 40–41
 - successful, characteristics of, 10–12
 - tips for, 299
 - See also* Planning a Career; What Went Wrong?
- Entrepreneurship
 - advantages, 14
 - aptitude, assessing, 14
 - are you right for?, 13–15
 - defined, 5
 - disadvantages, 14–15
 - goal setting, 19–20
 - ideas, looking for, 16–17
 - interests, assessing, 13–14
 - investigate opportunities, 18
 - real-life lessons learned, 35
 - self-assessment for, 13–15
 - U.S. economy and, 3, 4
 - See also* Businesses
- Entrepreneurship Business Plan Competition, 209
- Environment
 - laws governing, 377
 - respecting, 376–377
- Environmental Protection Agency (EPA), 377
- EPA. *See* Environmental Protection Agency (EPA)
- Equal Employment Opportunity Commission (EEOC), 313
- Equilibrium price and quantity, 50
- Equipment, obtaining, 224–226
- Equity, 239
- Equity capital, 240–241
- Esteem needs, 37
- Ethics
 - codes of, 371, 372–373
 - culture and, 370–371
 - defined, 370
 - See also* Business ethics
- Exclusive Concepts, 35
- Executive summary, of business plan, 75–76
- Existing business
 - family business, 184–185
 - purchasing, 178–180
 - See also* Franchise
- Expansion. *See* Growth strategies
- Experience
 - lack of, as reason for loan refusal, 244
 - as source of business ideas, 17
 - summarized in business plan, 71
- Exporter's Encyclopedia* (Dunn and Bradstreet), 380, 381
- Exporting, 378–379

F

- Factors of production, 39
- Failure, factors in, 9

- Fair Credit Billing Act, 199
- Fair Labor Standards Act (FLSA), 313
- Family business, 184–185
- Family Medical Leave Act (FMLA), 314
- Famous Entrepreneur
 - Barge, Anne, 167
 - Brin, Sergey, 122
 - Disney, Walter Elias, 67
 - Edison, Thomas A., 98
 - Ganz Family, 281
 - Griffin, Merv, 351
 - Pag, Johnny, 383
 - Page, Larry, 122
 - Ray, Rachel, 221
 - Revere, Paul, 44
 - Rowling, J.K., 312
 - Walker, Madam C.J., 7
 - Whitney, Eli, 197
 - Wright Brothers, 243
- Faruk, Omar, 299
- FBLA. *See* Future Business Leaders of America (FBLA)
- FDA. *See* Food and Drug Administration (FDA)
- Features. *See* Product features
- Federal Food, Drug, and Cosmetic Act, 198
- Federal Trade Commission (FTC)
 - Franchise and Business Opportunity Rule, 181
 - protection of competition by, 195–196
- Feedback, customer loyalty and, 109
- Finance
 - careers in, 266
 - function of business, 48
- Finance charge, 198–199
- Financial analysis, in new product development, 368
- Financial goals, 19
- Financial institutions, 80
- Financial management, information in business plan, 72–73. *See also* Financial statements
- Financial projections, 81
- Financial statements
 - analyzing, 286–290
 - breakeven analysis, 290
 - in business plan, 73
 - cash flow, 287
 - income, 287
 - net profit on sales analysis, 288–289
 - preparing, 286–287
 - profit goals, 289
 - sales analysis, 287–288
 - See also* Pro forma financial statement
- Financing
 - assess your financial needs, 238–240
 - business plan as aid in, 66–67, 73
 - commercial bank loans, 242–244
 - debt capital, 241–245
 - equity capital, 240–241
 - friends and relatives, 241–242
 - government agency loans, 244–245
 - personal contributions, 240
 - personal financial statement, 239–240
 - startup costs, 239
 - venture capitalists, 241
- Five Cs of Credit (character, capacity, capital, collateral, conditions), 63
- Five P's of entrepreneurship (planning, persistence, patience, people, profit), 91
- Fixed assets, 251
- Fixed costs, 51
- Floating ad, 155
- Flood insurance, 341
- Floor plan, 220
- FLSA. *See* Fair Labor Standards Act (FLSA)
- FMLA. *See* Family Medical Leave Act (FMLA)
- Focus groups, market research through, 99
- Focus on Economics, 36, 42, 49
- Focus on Small Business, 4, 10, 16, 21, 64, 69, 78, 92, 97, 104, 120, 126, 131, 148, 154, 164, 178, 187, 194, 210, 218, 224, 238, 246, 253, 270, 276, 283, 300, 307, 315, 332, 338, 345, 362, 370, 378
- Food and Drug Administration (FDA), 198
- Forbes* magazine, 181
- Ford Motor Co., 155, 184
- Ford Motor Company Fund, 375
- Forecasted receipts and disbursements, 247
- 401(k) plans, 312
- 4Teens Network, LLC, 3
- Franchise
 - advantages, 183
 - advertising fees, 181
 - careers in, 206
 - defined, 180
 - disadvantages, 183–184
 - disclosure documents, 181–182
 - evaluating, 182
 - initial fee, 181
 - investigating, 181
 - operating costs, 181
 - ownership of, 180–184
 - royalty fees, 181
 - start-up costs, 181
- Franchisee, 180
- Franchise Opportunities Handbook, The*, 180
- Franchisor, 180, 182, 183, 184
- Fraud, credit card, 336
- Freedom of choice, 45
- Free enterprise, 45

Freelancers, 305
 Friends, as source of business financing,
 241–242
 FTC. *See* Federal Trade Commission (FTC)
 Functions, job tasks, 301
 Functions of business, 47–48
 Funding, discussed in business plan, 73
 Future Business Leaders of America (FBLA).
 See WinningEdge

G

GadgetSleeves, 237
 Gagwear, 331
 Gamson, Jordy, 331
 Ganz, Samuel, 281
 Ganz Toys, 281
 GasBuddy.com, 38
 Gates, Bill, 3, 17
 General journal, 254
 General Motors, 155
 Geographic data, 95
 Geographic expansion, 365
 Global trends and opportunities. *See*
 International business
 Goals, 11
 in business plan, 70
 financial, 19
 long-term, 123
 marketing strategy and, 121–123
 medium-term, 123
 nonfinancial, 19–20
 profit, setting and meeting, 289
 setting, 19–20
 short-term, 122–123
 SMART (specific, measurable, attainable,
 realistic, timely), 19
 Goods
 defined, 38–39
 receiving, to sell, 152–153
 retail channels of distribution, 150
 transportation of, 151–152
 See also Products
 Goodwill, 179
 Google, 122
 Government agencies
 loans from, 244–245
 protection of competition by, 195–196
 Government regulation/protections
 of competition, 195–196
 of employees, 313–314
 of environment, 377
 of intellectual property, 196–197
 of international trade, 382–384
 Grants, from corporations, 375

Griffin, Merv, 351
 Gross lease, 219
 Gross profit, 250
 Gross sales, 288
 Growth stage, of product life cycle, 366
 Growth strategies
 choosing a strategy, 364–365
 controlling your growth, 363–364
 determining when to expand, 362–363
 product life cycle and development,
 366–369

H

Handling (of products), 152
 Harpo Productions, Inc., 8
 Health insurance, 312
 Hendricks, Brian, 91
 Hierarchy of needs (Maslow), 37
 Hiring
 interviewing candidates, 308–309
 making a job offer, 309
 reviewing and verifying job applications, 308
 screening candidates, 307–308
 See also Compensation package
 Hobbies, 16–17
 Home-based businesses, 214–215
 Home Depot, The, 7–8
 HUD. *See* Department of Housing and Urban
 Development (HUD) grants
 Human resources
 alternatives to adding staff, 305–306
 applying leadership styles, 316
 compensation package, 310–312
 controlling, 320–322
 defined, 39, 300
 delegating responsibility, 319
 directing, 315–318
 dismissing employees, 322
 enforcing employee policies, 316–317
 evaluating employees, 320, 321
 hiring, 307–309
 implementing your staffing plan, 315–318
 listening to employees, 319
 motivating employees, 318–319
 promoting employees, 320
 recruiting, 303–305
 regulations that protect employees, 313–314
 staffing, 300–303
 training employees, 317–318
 understanding management levels, 316
 Human risks, 332
 Human services careers, 32
 Hunt, Leo, 72
 Hurricane Katrina, 333, 339

I

- IBM, 105
- Icebox, The, 331
- Ideas
 - businesses born from, 63, 65, 70
 - defined, 16
 - development of, 367
 - screening of, 367–368
 - where to find, 16–17
- Ideas in Action
 - Capitalize on Youth Marketing, 177
 - Electronic Safekeeping, 237
 - Entertaining and Planning, 269
 - Growth is Risky, 331
 - Making Job Connections, 3
 - A Neighborhood Business, 209
 - Serving Customers' Needs, 91
 - Starting Young and Moving Up, 361
 - Turning a Bad Experience into a Million Dollars, 147
 - Turning an Idea into a Business, 63
 - Turning Creative Fun into Dollars, 119
 - Web Site Design, 35
 - Working for What You Believe In, 299
- IGD company, 220
- Immigration Reform and Control Act, 313
- Implementing, in organizing, 272–273
- Importing, 379
- Inc.* magazine, 181
- Income, irregular, 14
- Income statement, 249–250, 287, 289
- Income tax, 259
- Incorporate, 191–192
- Independence, 11
- Indirect channel of distribution, 149
- Indirect competition, 106
- Indirect exporting, 379
- Industrial businesses, location of, 214
- Industrial park, 214
- Industry, description in business plan, 71
- Inelastic demand, 50
- Infomercials, 157
- Information gathering, 22
- Information technology, careers in, 296
- Initial franchise fee, 181
- Installment loan, 347
- In-store advertising, 305
- Insurable risk, 339
- Insurance
 - accident, 312
 - business, 341–342
 - business interruption, 342
 - business owner's policy (BOP), 341–342
 - buying, 343–344
 - careers in, 358
 - choosing an agent, 343
 - coverage, 343–344
 - crime, 342–343
 - dental, 312
 - as employee benefit, 312
 - flood, 342
 - health, 312
 - on inventory, 280
 - as job benefit, 312
 - liability protection, 342
 - life, 312, 342
 - property, 341
 - renter's, 343
 - workers' compensation, 349–350
- Intellectual property, 196–197
- Interest, on unsold inventory, 280
- Interests
 - assessing, 13–14
 - as source of business ideas, 16–17
- Intermediaries, 149
- Intermediate-range planning, 271
- Internal Revenue Code, S corporation
 - organization under, 192
- International business
 - business plan for, 381
 - cultural diversity and, 353
 - exporting, 378–379
 - government assistance for, 383–384
 - government regulation for, 382–384
 - importing, 379
 - market analysis, 380–381
 - pros and cons, 350–352, 380
 - risks in, 350–352
 - selling worldwide through the Web, 379
- International Trade Administration, 384
- Internet
 - business plan information on, 80–81
 - distribution through, 150
 - for investigation of opportunities, 18
 - marketing through, 169
 - selling worldwide through the Web, 379
 - supplier identification through, 225
 - See also* World Wide Web
- Interns, 305
- Interviews
 - of job candidates, 308–309
 - rules for, 309
 - sample questions, 309
- Introduction, to business plan, 70–71
- Introduction stage, of product life cycle, 366
- Introductory elements, of business plan, 74–76
- Introductory pricing, 136
- Inventions, 17

Inventory

- carrying costs, 280
- costs of being out of stock, 281
- defined, 224, 276
- determining, 282
- interest on, 280
- management concerns, 276–277
- managing, 280–282
- for ongoing businesses, 227
- periodic method, 279
- perpetual method, 278–279
- physical, 279–280
- purchasing, 226–227
- purchasing plan, 277–278
- for startup business, 226–227
- stock turnover rate, 281–282
- tracking, 278–280

Inventory financing, 243

J

- Jensen, Erik and Andrew, 269
- Jibbitz, 119
- Job, 301
- Job analysis, 301–302
- Job applicants
 - interviewing, 308–309
 - offering job to, 309
 - screening, 307–308
- Job attributes checklist, 14
- Job creation, by entrepreneurs, 40–41
- Job description, 301–302
- Job interview, 308–309
- Job offer, 309
- Johnson & Johnson, 155
- Journals, 254
- Justice Department, 195–196
- Jx2 Productions, 269

K

- Kasner, Edward, 122
- KFC, 25

L

- Labeling, 129
- Landlord, 219
- Landscape architecture, careers in, 88
- Latin Artist, 63
- Lawrence, Jasmine, 147
- Lawyers, 199–200
- Layout
 - floor plan, 220
 - manufacturing business, 222–223
 - retail business, 220–222

- service business, 222
- wholesale business, 222

Leadership skills, 291

Leadership styles, 316

Lease

- of business space, 218–219
- commercial, 218–219
- costs and benefits of, 219
- gross, 219
- net, 219
- percentage, 219

Ledgers, 254–255

Legal forms of business

- corporation, 191–193
- limited liability company (LLC), 193
- partnership, 188–190
- S corporation, 192–193
- sole proprietorship, 187–188

Legality, of a contract, 200

Legal structure, in business plan, 70

Lelia College, 7

Letters

- business, 26–27
- cover letter for business plan, 74

Liabilities/liability

- current, 251
- defined, 239, 250
- long-term, 251

Liability insurance, 342

Library, for investigation of opportunities, 18

Licenses, 198

Life insurance, 312, 342

Lighting, retail business, 221

Limited liability company (LLC), 193

Line of credit, 242

Listening

- to employees, 319
- for maintaining customer loyalty, 109
- during telephone conversation, 201

Loans

- commercial bank, 242–244
- from friends and relatives, 241–242
- government agency, 244–245
- installment, 347
- long-term, 242
- reasons for refusal of, 243–244
- secured, 242–243, 347
- Small Business Administration (SBA), 244, 245
- unsecured, 243, 347

Local factors, as uninsurable risk, 341

Local governments, loans from, 245

Location

- community shopping centers, 211–212
- description in business plan, 71

- downtown, 210–211
- evaluation of, 216–217
- home-based businesses, 214–215
- industrial businesses, 214
- neighborhood shopping centers, 211
- nonretail business, 213–215
- regional shopping centers, 212
- retail business, 210–213
- service businesses, 213–214
- site selection, 216–217
- stand-alone stores, 212–213
- super-regional shopping centers, 212
- warehouses, 213
- LogicLotus, 299
- Long-term goals, 123
- Long-term liabilities, 251
- Long-term loan, 242

M

- Magazine advertising, 159–160
- Make Academic Connections
 - Career Success, 15
 - Communication, 9, 20, 30, 41, 54, 59, 68, 77, 86, 96, 103, 110, 125, 130, 138, 142, 153, 168, 172, 186, 200, 204, 217, 228, 232, 245, 260, 264, 275, 282, 294, 322, 337, 344, 352, 357, 377, 388
 - Economics, 48, 54, 59
 - Geography, 96, 153, 205
 - History, 30, 205
 - Language Arts, 82
 - Management, 68, 103, 110, 115, 193, 352
 - Marketing, 168, 172
 - Math, 9, 15, 20, 25, 30, 48, 58, 77, 82, 96, 114–115, 125, 138, 142, 143, 163, 173, 193, 204, 223, 228, 232–233, 245, 252, 260, 264, 282, 290, 294–295, 314, 326, 337, 344, 357, 369, 377, 384, 388–389
 - Problem Solving, 25, 48, 143, 163, 217, 252, 275, 290, 295, 306, 327
 - Research, 86, 115, 130, 172, 186, 200, 204–205, 223, 228, 232, 306, 314, 377, 384, 389
 - Social Studies, 9, 20, 41
 - Technology, 110
- Mall of America, 212
- Management
 - defined, 270
 - as function of business, 47
 - levels of, 316
- Management styles, 272–273
- Manager, 270
- Manpower, Inc., 304

- Manufacturing businesses, 5, 6
 - channels of distribution for, 149–151
 - defined, 5
 - layout design, 222–223
 - types of, 6
- Marcus, Bernie, 7
- Marginal benefit, 51–52
- Marginal cost, 51–52
- Markdown price, 134, 137
- Market
 - competitive, 53
 - customer profile and, 95–96
 - identifying, 92–96
 - prices and structure of, 52–54
 - researching, 97–103
 - target, 81, 92–93
 - See also* Competition
- Market analysis, international, 380–381
- Market development, 365
- Market economy
 - defined, 43
 - functions of business in, 47–48
- Marketing
 - defined, 120
 - as function of business, 47
 - information in business plan, 71–72
 - of new products, 369
 - real-life lesson about, 35
- Marketing concept
 - defined, 121, 126
 - product and, 126–127
- Marketing goals
 - long-term, 123
 - marketing plan and, 124–125
 - medium-term, 123
 - short-term, 122–123
- Marketing mix
 - defined, 47, 121
 - distribution, 148–153
 - price, 131–138
 - product, 126–130
 - promotion, 154–163
- Marketing plan, 124–125
- Marketing strategy
 - defined, 121
 - dollars spent annually, 127
 - long-term goals, 123
 - medium-term goals, 123
 - requirements of, 121–122
 - short-term goals, 122–123
- Market penetration, 365
- Market research
 - careers in, 116
 - defined, 97

- Market research (*Continued*)
 - disadvantages of primary data, 99
 - focus groups in, 99
 - observation in, 98
 - primary data in, 97–99
 - secondary data, 99
 - steps in, 100–103
 - surveys in, 98
 - Market segments
 - customer profile and, 95–96
 - defined, 94
 - importance of, 94–95
 - Market share
 - defined, 132
 - as pricing objective, 132–133
 - Market structure
 - defined, 52
 - monopolistic competition, 53
 - monopoly, 54
 - oligopoly, 53
 - perfect competition, 52
 - prices and, 52–54
 - Markup price, 134
 - Maslow, Abraham, 37
 - Maslow's Hierarchy of Needs Pyramid, 37
 - Mass production, 197
 - Maturity stage, of product life cycle, 366
 - McClure, Dave, 53
 - Medical insurance. *See* Health insurance
 - Medium-term goals, 123
 - Mentoring, 317
 - Mentorship, 35
 - MESBICs. *See* Minority Enterprise Small Business Investment Companies (MESBICs)
 - Mexico, NAFTA and, 383
 - Microsoft, 17
 - Middle-management level, 316
 - Minimum wage, 311, 313
 - Mining and extracting businesses, 5
 - Minority Enterprise Small Business Investment Companies (MESBICs), 244
 - Mistakes, learning from, 24–25
 - Mixed economy, 44
 - Mixed management style, 272–273
 - Monopolistic competition, 53
 - Monopoly, 54
 - Monster.com, 304
 - Motiva International, 318
 - Motivation
 - of employees, 318–319
 - of entrepreneurs, 11
 - Multimedia presentations, 117
 - Multiple-unit pricing, 137
 - Municipal governments, loans from, 245
- N**
- NAFTA. *See* North American Free Trade Agreement (NAFTA)
 - National Federation of Independent Businesses (NFIB), 284
 - National Foundation for Teaching Entrepreneurship (NFTE), 147, 209, 299
 - National Philanthropic Trust, 375
 - National Safety Council, 333
 - Natural resources, 39
 - Natural risks, 332
 - Needs
 - about, 36–38
 - of customers, serving, 91
 - determining, in selling, 166–167
 - Needs assessment, 166
 - Need satisfying, 166
 - Neighborhood shopping centers, 211
 - NET Bookmark
 - advertising history, 157
 - brand or product name, 129
 - franchises, 183
 - gasoline prices, Web sites for, 38
 - management styles, 272
 - Manpower, Inc., employment agency, 304
 - market segmentation, 101
 - recognizing opportunity, 17
 - robbery awareness, 335
 - Small Business Administration (SBA)
 - loans, 244
 - social responsibilities, 374
 - store layouts, 222
 - teen entrepreneurs, 81
 - Net cash flow, 247
 - Net income after taxes, 288–289
 - Net income before taxes, 250
 - Net income from operations, 288–289
 - Net income/loss after taxes, 250
 - Net lease, 219
 - Net profit on sales
 - analyzing, 288–289
 - importance of, 289
 - Net sales, 288
 - Networking, 133
 - Net worth, 239, 250, **252**
 - New product development. *See* Product development
 - News Corp., 155
 - Newspaper advertising, 158
 - NFIB. *See* National Federation of Independent Businesses (NFIB)

NFTE. *See* National Foundation for Teaching Entrepreneurship (NFTE)
 Nike, 129
 Nilsson, George, 161
 Nonfinancial goals, 19–20
 Nonretail businesses, location of, 213–215
 North American Free Trade Agreement (NAFTA), 383

O

Objectives, of business plan, 65
 Observation, market research through, 98
 Obsolescence, 280
 Occupational Safety and Health Act (OSH Act) of 1970, 313
 Occupational Safety and Health Administration (OSHA), 313, 333
 Odd/even pricing, 137
 Office of International Trade of the Small Business Administration, 383–384
 Office of Special Counsel for Immigration-Related Unfair Employment Practices, 313
 Oligopoly, 53
 Online advertising
 disadvantages of, 156
 paying for, 156
 types of, 155–156
 Online career and employment sites, 304
 Online resources, for research, 80–81
 On-the-job training, 317
 Operating costs, franchise, 181. *See also*
 Operating expenses
 Operating expenses, 250
 Operating policies, 274
 Operating procedures
 controlling, 273
 customer service policies, 274
 delivery policies, 274
 implementing, 272–273
 management functions, 270–273
 operating policies, 274
 operations manual, 273–275
 organizing, 271
 planning, 270–271
 safety policies, 275
 staffing, 272
 Operations, information in business plan, 73
 Operations management
 financial management, 283–290
 inventory management, 276–282
 operating procedures, 270–275
 See also individual topics

Operations manual
 customer service policies, 274
 defined, 273
 delivery policies, 274
 operating policies, 274
 rules, policies, and procedures, 273
 safety policies, 275
 Opportunities
 comparing, 18
 defined, 16
 investigating, 18
 recognizing, 6–8
 Opportunity cost, 46–47
 Organizational chart, 271, 302
 Organizational structure, 271, 302–303
 Organizing, 271
 OSHA. *See* Occupational Safety and Health Administration (OSHA)
 Outdoor advertising, 160
 Outstanding checks, 257–258
 Overtime work, 313
 Owner's equity, 250
 Ownership style, in business plan, 70. *See also*
 Legal forms of business

P

Packaging, 128, 129, 152
 Pag, Johnny, 383
 Page, Larry, 122
 Paid advertisements, 157
 Paid leave, 311
 Participatory management, 272
 Partnership, 70
 advantages, 188
 defined, 188
 disadvantages, 188
 Partnership agreement, 188–190
 Pascarella, Joseph, 361
 Patent pending, 196
 Patents, 196
 Pay, types of, 310–311
 Payroll
 defined, 258
 records for, 258–259
 reducing, 286
 register, 258–259
 Payroll, as business expense, 286
 Payroll deductions, 259
 Payroll taxes, 259
 Penetration pricing, 136
 Pension plans, 312
 Percentage lease, 219
 Perfect competition, 52
 Performance evaluation, 320, 321

- PerioDent Company, 161
- Periodic inventory method, 279
- Perpetual inventory method, 278–279
- Perseverance, 11, 35
- Personal contributions, in business
 - financing, 240
- Personal debt, avoiding, 53
- Personal financial statement, 239–240
- Personal selling
 - defined, 165
 - product knowledge, 165
- Physical distribution
 - defined, 151
 - packaging, 152
 - product storage and handling, 152
 - receiving goods to sell, 152–153
 - transportation, 151–152
- Physical inventory, 279–280
- Physiological needs, 37
- Picture-Perfect cosmetics, 364
- Planning, 270–271
- Planning a Career
 - architecture and construction, 234
 - audio-video technology, 328
 - e-marketing, 144
 - finance, 266
 - franchising, 206
 - human services, 32
 - information technology, 296
 - insurance, 358
 - landscape architecture, 88
 - marketing researcher, 116
 - property management, 60
 - public safety, 174
 - transportation, 390
- Point-of-sale (POS) software system, 279
- Policies, 273
- Pop-under ad, 156
- Pop-up ad, 155
- Positioning, 129–130
- Posting, 254–255
- Premium, insurance, 338
- Presentation skills, 55
- Press release, 161
- Prestige pricing, 136
- Price lining, 137
- Prices
 - defined, 131
 - determining, for a product, 134–135
 - determining, for a service, 135–136
 - equilibrium, quantity and, 50
 - markdown, 134, 137
 - market structure and, 52–54
 - markup, 134
 - price wars, 94
 - See also* Pricing
- Price skimming, 136
- Pricing
 - breakeven point, 139
 - bundling of services and, 136
 - competition-based, 134–135
 - cost-based, 134
 - demand-based, 134
 - discount, 137–138
 - introductory, 136
 - market share and, 132–133
 - objectives, setting, 131–133
 - psychological, 136
 - return on investment (ROI) and, 132
 - time-based, 135–136
 - See also* Price
- Primary data
 - defined, 97
 - disadvantages of, 99
 - types, 98–99
- Print resources, for research, 80
- Private property, 45
- Problem resolution, in selling, 166
- Problem solving
 - process for, 21–23
 - skills for, 24–25
- Procedures, 273
- Procter & Gamble, 155
- Product development
 - financial analysis, 368
 - idea development, 367
 - idea screening, 367–368
 - marketing, 369
 - prototype and testing, 368
 - strategy development, 368
 - See also* Product life cycle and development
- Product features, 128–129, 165
- Production
 - factors of, 39
 - as function of business, 47
- Product knowledge, 165
- Product life cycle and development
 - decline stage, 366
 - growth stage, 366
 - introduction stage, 366
 - maturity stage, 366
 - new product development, 367–369
 - See also* Product development
- Product mix, 127
- Products
 - analyzing sales by, 287–288
 - description in business plan, 71
 - diversification and, 365

- knowledge of, 165
- marketing concept and, 126–127
- marketing mix and, 126–130
- positioning and, 129–130
- selecting features of, 128–129
- Product storage, 152
- Professional consultants, 80
- Profit, 45
- Profit/loss statement. *See* Income statement
- Profit sharing, 310
- Pro forma financial statements, 73
 - balance sheet, 250–252
 - cash flow statement, 246–248
 - defined, 239
 - income statement, 249–250
 - See also* Financial statements
- Promotional mix, 154
- Promotional pricing, 137
- Promotion, of employees, 320
- Promotion, of products and services
 - advertising, 154–160
 - consumer needs and wants, 166–167
 - personal selling, 165
 - publicity, 161–163
 - rebate, 168
 - sales promotion, 168
 - telemarketing, 168
 - See also individual topics*
- Property insurance, 341
- Property management, careers in, 60
- Proposals, from vendors, 225–226
- Prototype, 368
- Provisional patent application, 196
- Psychographics, 95
- Psychological pricing, 136
- Publicity
 - defined, 161
 - press release, 161
 - public relations, 162
 - self-promotion, 163
- Public relations, 162
- Public safety, careers in, 174
- Purchases journal, 254
- Purchasing
 - equipment and supplies, 224–226
 - inventory, 226–227
- Purchasing plan, inventory and, 277–278
- Pure risk, 338–339

Q

- Qualitative restriction, 382
- Quantity, 50
- Quantity discounts, 138

- Quota, 382
- Quote, as purchase estimate, 226

R

- Radio advertising, 157–158
- Rapappy, Inc., Personalized Headbands and Wristbands, 209
- Rational buying decisions, 166
- Ray, Rachel, 221
- Rebate, 168
- Receipts, 247
- Receiving goods to sell, 152–153
- Reconciling a bank statement, 257–258
- Recordkeeping, 253–260. *See also* Records
- Records
 - aging tables, 255
 - banking, 256–258
 - journals, 254
 - ledgers, 254–255
 - payroll, 258–259
 - subsidiary ledgers, 255
 - tax, 259–260
- Recovery plan, 333
- Recruiting, for job positions
 - classified advertisements, 303
 - college placement centers, 304
 - defined, 303
 - employment agencies, 304
 - in-store advertising, 305
 - online career and employment sites, 304
 - referrals, 305
- Referrals, for jobs, 305
- Regional shopping centers, 212
- Regulation, government. *See* Government regulation/protections
- Relatives, as source of business financing, 241–242
- Rent, calculating, per customer, 219
- Renter's insurance, 343
- Reorder point, 227, 279
- Repetitive stress injuries, 348
- Research
 - for business plan, 72, 78–81
 - insufficient, 81
 - of international market, 380–381
- Resource allocation, 271
- Resources
 - capital, 39
 - economic, 38–40
 - limited, 39–40
 - natural, 39
 - See also* Human resources
- Resume, 261

- Retailing businesses
 - channels of distribution for, 149–150
 - competition and, 107
 - defined, 5
 - layout design, 220–222
 - location of, 210–213
 - types of, 6
- Retail price, 134–135
- Retirement plans, 312
- Return on investment (ROI)
 - defined, 132
 - discussed in business plan, 73
 - as pricing objective, 132
- Revenue, 249
- Revere, Paul, 44
- Revere Copper and Brass, Inc., 44
- Review Your Knowledge, 29–30, 57–58, 85–86, 113–114, 141–142, 171–172, 203–204, 231–232, 263–264, 293–294, 325–326, 355–356, 387–388
- Risk
 - classification of, 338–340
 - controllable, 339
 - of credit, 345–348
 - defined, 332
 - discussed in business plan, 73
 - economic, 332
 - on entrepreneurship, 14
 - human, 332
 - identifying, 332
 - insurable, 339–340
 - in international business, 350–352
 - natural, 332
 - preparing to face, 333–334
 - pure, 338–339
 - speculative, 339
 - theft as, 335–337
 - uncontrollable, 339
 - uninsurable, 339–341
 - at work, 348–350
- Risk assessment, 333
- Risk management, 332. *See also* Insurance; Theft
- Robbery, 335, 336
- Robinson-Patman Act, 195
- Rodriguez, Jeffrey, 63
- Rowling, J.K., 312
- Royalty fees, for a franchise, 181
- Rules, 273
- S**
- Safety policies, 275
- Safe working conditions, 313
- Salary, 310. *See also* Wages
- Sales
 - analyzing, 287–288
 - breakeven analysis and, 290
 - gross, 288
 - net, 288
 - net profit on, 288–289
- Sales journal, 254
- Sales promotion, 168
- Sales tax, 260
- Sanders, Colonel, 25
- SBA. *See* Small Business Administration (SBA)
- SBDCs. *See* Small Business Development Centers (SBDCs)
- Scanners, 99
- Scarcity, 46
- Schmelzer, Sheri and Rich, 119
- Schultz, Howard, 7
- SCORE. *See* Service Corps of Retired Executives (SCORE)
- S corporation, 192–193
- Screening, of job candidates, 307–308
- Seasonal discounts, 138
- Secondary data, 99, 106
- Secured loans, 242–243, 347
- Security needs, 37
- Self-actualization needs, 37
- Self-assessment, for entrepreneurship, 13–15
- Self-confidence, 11
- Self-promotion, 163
- Selling, 164–165. *See also* Personal selling
- Seminars, as employee training, 317
- September 11, 2001, 340
- Serrano, John, 63
- Service businesses
 - channels of distribution for, 150–151
 - defined, 5
 - layout design, 222
 - location of, 213–214
 - types of, 6
- Service Corps of Retired Executives (SCORE), 79, 80
- Service, customer loyalty and, 109–110
- Services
 - bundling, 136
 - defined, 38–39
 - description in business plan, 71
 - diversification and, 365
 - positioning, 129–130
 - pricing, 135–136
- Shareholders, 191, 192
- Share of stock, 191
- Sharpen Your Entrepreneurial Skills
 - breakeven point, 139
 - business letters, 26–27

- cultural diversity, 353
- data analysis with spreadsheets, 111
- e-mail etiquette, 229
- leadership skills, 291
- marketing and the Web, 169
- presentation skills, 55
- resume, 261
- teamwork, 323
- telephone conversations, 201
- time management, 385
- using technology tools, 83
- Shea, Katelin, 237
- Sherman Act, 195
- Shills, 182
- Shoplifting, 335
- Shopping centers
 - community, 211–212
 - neighborhood, 211
 - regional, 212
 - super-regional, 212
- Short-term goals, 122–123
- Short-term planning, 271
- Sick leave, 311
- Site selection, 216–217
- Skills
 - leadership, 291
 - presentation, 55
 - problem-solving, 24–25
 - speaking, 89
 - summarized in business plan, 71

See also Sharpen Your Entrepreneurial Skills
- Small Business Administration (SBA)
 - as business research source, 79
 - entrepreneurial business chart, 6
 - information published by, 80
 - international trade statistics from, 380
 - for investigation of opportunities, 18
 - loans from, 244, 245
 - Office of Advocacy, 6, 8
 - Office of International Trade, 383–384
 - secondary data from, 99
- Small Business Development Centers (SBDCs), 79
- Small Business Investment Companies (SBICs), 244
- SMART (specific, measurable, attainable, realistic, timely) goals, 19, 122
- Smigler, Scott, 35
- Social needs, 37
- Social responsibilities
 - to community, 375–376
 - to creditors, 375
 - to customers, 374
 - to investors, 375
 - personal, 373
 - to suppliers, 374–375
- Software
 - for business plan, 83
 - point-of-sale, 279
- Sole proprietorship, 70
 - advantages, 187–188
 - defined, 187
 - disadvantages, 188
- Solutions, identifying, 22–23
- Soviet Union, 44
- Space, lease or buy, 218–219
- Spamming, 156
- Speaking skills, 89
- Speculative risk, 339
- Spreadsheets, 111, 284
- SQ3R (survey, question, read, recall, review)
 - method, 333
- Staff. *See* Employees
- Staffing
 - alternatives to adding staff, 305–306
 - defined, 272, 301
 - implementing your plan, 315–318
 - job descriptions, 301–302
 - organizational structure, 302–303
 - recruiting, 303–305

See also Hiring
- Stahl, Mike, 3
- Stand-alone stores, 212–213
- Starbucks Coffee Company, 7
- Startup businesses
 - inventory for, 226–227
 - loans declined for, 243–244
- Startup costs, 181, 239
- StartUpPC, 91
- State governments, loans from, 245
- Statement of purpose, in business plan, 75
- Stereotyping, 353
- Stevens, Sarah-Jane, 364
- Stock, corporate, 191
- Stock card, 278–279
- Stockholders, 191, 192
- Stock turnover rate, 281–282
- Storage of inventory, 280
- Strategic planning, 271
- Strauss, Levi, 3
- Subsidiary ledgers, 255
- Success
 - entrepreneurial characteristics for, 10–12
 - factors in, 8–9
- Supermarkets, 212
- Super-regional shopping centers, 212
- Supervisory management level, 316

Suppliers
 credit terms, 286
 of existing business, 179
 identifying, 225
 responsibilities to, 374–375
 See also Vendors
 Supplies, obtaining, 224–226
 Supply
 curve, 50
 defined, 49–50
 Supply and demand, 40
 curves, 50
 demand, defined, 50
 equilibrium price, quantity, and, 50
 supply, defined, 49–50
 Survey
 design of, 101
 for market research, 98
 sample, 102

T

Table of contents, of business plan, 75
 Target Corporation, 374
 Target markets
 competition and, 105
 customer profile and, 95–96
 defined, 92
 defining, 81
 identifying, 93
 Tariff, 382
 Task assignment, 271
 Taxes
 net income after, 288–289
 net income before, 250
 net income/loss after, 250
 sales, 260
 Tax records, 259–260
 Taylor, Ephren, Jr., 3
 Teams, member characteristics, 12
 Teamwork, 323
 Technology
 for business plan, 83
 changes in, as uninsurable risk, 341
 e-mail etiquette, 229
 for inventory tracking, 279
 keeping up with, 11
 marketing and the Web, 169
 online career and employment sites, 304
 selling worldwide through the Web, 379
 spreadsheets, 111, 284
 See also Internet; Web sites; World Wide Web
 Teen entrepreneurs, 81, 91
 Telemarketing, 168

Telephone conversations, effective, 201
 Telephone directory advertising, 158, 225
 Television advertising, 156–157
 Temporary workers, 306
 Tenant, 218–219
 Theft
 bounced checks, 337
 credit card fraud, 336
 by employees, 335–336
 robbery, 336
 shoplifting, 335
 Theory X managers, 316
 Theory Y managers, 316
 Think About It, 9, 15, 20, 25, 41, 48, 54, 68, 77, 82, 96, 103, 110, 125, 130, 138, 153, 163, 168, 186, 193, 200, 217, 223, 228, 245, 252, 260, 275, 282, 290, 306, 314, 322, 337, 344, 352, 369, 377, 384
Thomas Register, The, 153
 Time-based pricing, 135–136
 Time management, 385
 Time Warner Inc., 155
 Title page, of business plan, 75
 Top-management level, 316
 Trade area, 216
 Trade associations, 80, 225
 Trade barrier, 382
 Trade credit, 346
 Trade discounts, 138
 Trade fairs, 380
 Trade magazines, 153, 225
 Trademarks, 197
 Tradeoff, 46
 Trade shows, 18
 Traditional economy, 43
 Training, 317–318
 Transaction, financial, 253–254
 Transit advertising, 160
 Transportation
 careers in, 390
 in channel of distribution, 151–152
 Trick banner, 155
 Trust, 194
 Truth-in-Lending Act of 1968, 198–199
 Turnover rates, of inventory, 281
 Twin Spin DJ and Entertainment, 269

U

U-Corp, 94
 Uncollectible accounts, 251–252, 348
 Uncontrollable risk, 339
 Uninsurable risk, 339–341

Universal product code (UPC), 99
 Unsecured loans, 243, 347
 U.S. Census
 secondary data from, 99
 trade statistics from, 380
 U.S. Department of Commerce, 380, 384
 Bureau of Industry and Security, 384
 Economic Development Administration (EDA) of, 245
 Franchise Opportunities Handbook, The, 180
 International Trade Administration, 384
 trade fairs and seminars, 380
 U.S. Department of Housing and Urban Development (HUD), 244–245
 Use-based data, 95
 U.S. economic system, 45, 104
 U.S. economy
 entrepreneurship and, 3, 4
 entrepreneurs' role in, 40–41
 family businesses in, 184
 U.S. Justice Department Antitrust Division, 195–196
 U.S. Occupational Health and Safety Administration. *See* Occupational Safety and Health Administration (OSHA)
 U.S. Patent and Trademark Office, 196
 U.S. Small Business Administration. *See* Small Business Administration (SBA)

V

Vacations, employee, 311
 Valuator, 180
 Variable costs, 51
 Vendors, 225–226. *See also* Suppliers
 Venture capitalists, 241
 Verizon, 155
 Vocabulary Builder, 29, 57, 85, 113, 141, 171, 203, 231, 263, 293, 325, 355, 387

W

Wages
 competitive, 311
 defined, 310
 laws governing, 313
 types of pay, 310–311
 Walker, Charles Joseph, 7
 Walker, Madam C.J., 7
 Wallpaper ad, 155
Wall Street Journal, 181
 Wal-Mart, 107, 147, 184
 Wal-Mart Foundation, 375
 Walt Disney Corporation, 67, 155
 Want ad, 303

Wants
 about, 36–38
 determining, in selling, 166–167
 Warehouses
 retail store, 213
 wholesale business in, 222
 Warren, Sandy, 318
 Web marketing, 169
 Web site design, 35
 Web sites
 gasoline prices on, 38
 for research, 80–81
 Webvan, 285
 Wells, Tina, 177
 Wells-Fargo Foundation, 375
 West Edmonton Mall, 212
 What Went Wrong?
 All Your Eggs in One Basket, 256
 Avoid Personal Debt, 53
 Dental Promotion Leaves Bad Taste, 161
 Do Market Research, 72
 Experience Needed, 13
 Goodbye, Gorgeous!, 342
 Makeup Test, 364
 Packaging Matters, 128
 Partnership Woes, 190
 Price War, 94
 Right Space, Wrong Place, 215
 Too Big, Too Fast, 285
 Whom Do You Trust?, 318
 What Would You Do?, 30, 59, 87, 115, 143, 173, 205, 233, 265, 295, 327, 357, 389
 Wheeler-Lea Act, 195
 Whitney, Eli, 197
 Whole Foods, 147
 Wholesalers, as intermediaries, 149
 Wholesaling businesses
 defined, 5
 layout design, 222
 types of, 6
 Williams, Ryan, 209
 Window displays, 221
 Winfrey, Oprah, 3, 8
 WinningEdge
 Business Professionals of America (BPA)
 Global Marketing Team Event, 145
 Prepared Speech Event, 89
 Presentation Management Team Event, 33
 Small Business Management Team Event, 391
 DECA (Delta Epsilon Chi)
 Business Law and Ethics Management Team Decision Making Event, 207

WinningEdge (*Continued*)

- Business Services Marketing Series Event, 359
- Buying and Merchandising Management Team Decision Making Event, 235
- Entrepreneurship Promotion Project, 175
- Future Business Leaders of America (FBLA)
 - Business Financial Plan, 267
 - Business Plan, 329
 - Emerging Business Issues Event, 61
 - Multimedia Presentation, 117
 - Partnership with Business, 297
- Women, as business owners, 11
- Workers' compensation, 349–350
- Workplace
 - antidiscrimination laws, 313–314
 - ethical, 372–373
- Workplace safety, 313

Work risks

- Federal Employee's Compensation Act (FECA), 348–349
- types of, 348
- workers' compensation, 349–350
- World Water Council, 46
- World Wide Web
 - distribution and, 150
 - exporting through, 379
 - recruiting employees with, 304
 - See also* Internet
- Wright, Wilbur and Orville, 243

Y

- Youth Entrepreneurship Expo, 209
- Youth Venture, 63

Z

- Zoning laws, 198

